THE HONORABLE JAMES L. ROBART

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

JONATHAN STUDEN, Individually and on Behalf of All Others Similarly Situated, Plaintiff, vs. FUNKO, INC., et al., Defendants.	No. 2:23-cv-00824-JLR CLASS ACTION FIRST AMENDED COMPLAINT FOR VIOLATIONS OF THE FEDERAL SECURITIES LAWS DEMAND FOR JURY TRIAL

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Lead Plaintiff Construction Laborers Pension Trust of Greater St. Louis ("Lead Plaintiff") and named plaintiff Paul Haddock (together, "Plaintiffs") allege the following against Funko, Inc. ("Funko" or the "Company"), Andrew Perlmutter ("Perlmutter") and Jennifer Fall Jung ("Fall Jung") (together, "Defendants"), by and through Lead Counsel Robbins Geller Rudman & Dowd LLP, upon personal knowledge as to themselves and their own acts, and upon information and belief as to all other matters.[1]

I. SUMMARY OF THE CASE

1. Plaintiffs bring this federal securities class action for violations of §§10(b) and 20(a) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§78j(b) and 78t(a), on behalf of themselves and all other similarly situated persons or entities (the "Class") who purchased or otherwise acquired the publicly traded Class A common stock of Funko between March 3, 2022 and March 1, 2023, inclusive (the "Class Period"), and were damaged thereby.

2. This case arises from pop culture product company Funko, its former Chief Executive Officer ("CEO") Andrew Perlmutter, and its former Chief Financial Officer ("CFO") Jennifer Fall Jung's reckless and materially false and misleading statements to investors concerning Funko's abysmal execution of two highly touted infrastructure projects and its accumulation of excess and obsolete inventory.

[1] Plaintiffs' information and belief is based on, among other things, the independent investigation of counsel, which includes, but is not limited to: (a) review and analysis of public filings made by Funko with the U.S. Securities and Exchange Commission ("SEC"); (b) review and analysis of press releases and other publications disseminated by Defendants; (c) review of news articles, securities analyst reports, and shareholder communications; (d) review of other publicly available information concerning Defendants; (e) accounts of former Funko employees and/or contractors; and (f) review of public filings and court orders in other litigation against one or more defendant, including *Ferreira v. Funko, et al.*, No. 2:20-cv-02319-VAP (PJWx) (C.D. Cal.). Many of the facts supporting the allegations contained herein are known only to Defendants named herein or are exclusively within their custody and control. Plaintiffs believe that substantial additional evidentiary support will exist for the allegations set forth herein after a reasonable opportunity for discovery.

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3. At the beginning of 2022, Funko had just completed a year of exceptional sales growth. Funko's flagship product, FunkoPop!s – stylized vinyl figurines based on licensed content from Disney, Marvel, LucasFilms, WarnerBros, and countless other pop culture intellectual property ("IP") holders – experienced a massive surge in popularity during the COVID-19 pandemic. At $15 a Pop!, with a wide-ranging set of characters available at any given time and new releases and exclusive Pop!s issued regularly, FunkoPop!s were perfect for both hobbyists looking to start or develop an existing collection, as well as for casual purchasers interested in a particular brand of pop culture fandom wanting to make an impulse purchase. Funko's business model was dependent on being able to develop new FunkoPop!s and other products quickly in order to (i) capitalize on TV show, movie, or video game releases and pop culture trends and (ii) make the most of its typical two-year license agreements. To that end, Funko prided itself on its ability to "go from product design of a figure to the store shelf within 110 to 200 days."

4. In order for Funko to continue its impressive growth trajectory, it needed to scale its operations – and that meant investing significantly in upgraded infrastructure. Back in 2020, Funko had begun planning to move from its antiquated enterprise resource planning ("ERP") software, designed for small- to mid-sized businesses, to a much more powerful and sophisticated Oracle platform that would provide enhanced functionality and analytics for all of Funko's various business processes across its global operations.

5. Designing the Oracle system to fit Funko's business needs was a substantial undertaking, and one that Funko was ill-prepared to complete. There was little alignment between Funko's top leadership as to what direction the project would take, and as of the start of the Class Period, there were critical decisions about the Oracle platform's design that were simply not being made. Without those decisions, the Company could not develop the necessary system architecture on the Oracle platform. More, the Oracle project had highlighted serious flaws in Funko's controls over its business data. In order for data to be transferred to the Oracle platform from Funko's existing ERP system, Microsoft NAV (also referred to as "NAV"), it first needed to be "cleaned"

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– checked for completeness, accuracy, and then conformed to the formatting and categorization system used by Oracle. Because Funko had never implemented any data governance controls, however, its data was a mess. There were no rules for who could input particular data, how that data should be entered into NAV, or what format should be used. As a result, the process of cleaning the data would require extensive effort and manhours from Funko employees in each area of business before their business data would be ready for transfer to Oracle. By February 2022, that process was nowhere close to being completed.

6. Funko's second major infrastructure upgrade planned for 2022 was the relocation and consolidation of its five Washington warehouses into one enormous, state-of-the-art distribution center in Buckeye, Arizona (the "Buckeye DC" or "DC"). Funko planned for the Buckeye DC to operate on its new Oracle platform's warehouse management software ("WMS"), which would use analytics and various inventory tracking tools to greatly enhance the efficiency and productivity of Funko's order fulfillment and distribution operations.

7. The Company knew that when Funko began its lease on the 850,000+ square foot facility in early April 2022, it would be a largely blank slate – Funko would have to build out the needed storage racks, office space, loading bays, and even bathrooms, and obtain all the necessary inspections and permits for each from the local building office along the way. Funko would also need to ship all of the inventory in its Washington warehouses down to Buckeye – an amount so substantial that it would take three months to truck it all down to the new DC. Among the inventory that Funko management had decided to ship to Buckeye were millions of units of "dead" inventory that could not be sold due to license expirations or simple lack of demand.

8. In each of its fourth quarter 2021 ("4Q21") and first quarter 2022 ("1Q22") Forms 8-K filed with the SEC, as well as during the Company's 4Q21 and 1Q22 earnings calls, Defendants asserted that Funko would move into its Buckeye DC in the second quarter of 2022 ("2Q22"), and implement its new ERP software by the beginning of the third quarter ("3Q22") or end of 2Q22. They also represented that as a result of these infrastructure projects, the Company's

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Selling, General and Administrative ("SG&A") expenses would result in 80 basis points of "pressure" on the Company's adjusted EBITDA margin,[2] but "for sure" only in the first half of the year. More, in its 4Q21 and 1Q22 Forms 10-Q filed with the SEC, Funko "warned" investors that if it did not manage its inventory levels appropriately, the Company could have to hold slow-selling or obsolete inventory for long periods of time or write down the cost of the inventory entirely. These statements misrepresented the facts as they were known inside the Company: that the ERP system implementation would not be possible by the end of 2Q22 or early 3Q22, that the costs of consolidating and relocating the Buckeye DC and the Oracle project could not "for sure" be limited to the first half of 2022 ("1H22"), and that Funko already had substantial amounts of obsolete and unwanted inventory collecting dust in its warehouses.

9. In late April 2022, trucks carrying Funko's inventory from its Washington warehouses began arriving at the Buckeye DC by the dozens. Unsurprisingly, the DC had not been fully built out yet, with storage racks still under construction and only 12 of 84 planned loading bays open for receiving product. The Company still hadn't purchased sufficient equipment needed to operate the massive warehouse: there was only one machine for the entire DC that could reach the top three to four shelves of Funko's newly built storage racks, a lack of scanning equipment for the "Receiving" teams unloading and putting away inventory from the truck trailers, and the belt systems purchased for unloading the trailers were too tall and largely unusable. The warehouse workers, a mix of employees from Funko's Washington warehouses, new hires, and temporary workers from an outside agency, had no usable Standards of Procedure ("SOPs") to instruct them as to the correct processes for handling inventory in the new DC. In fact, the new hires and temp workers were barely given any training before they were required to jump into

[2] An adjusted EBITDA margin is the ratio of a company's earnings before interest, taxes, depreciation and amortization to its revenues. Adjusted EBITDA margin is one of the most widely used metrics to assess a company's profitability.

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work. Worst of all, because the Oracle WMS that the entire DC had been designed around was not in place, the efficient layout, storage plan, and workflows planned were utterly useless.

10. As a result of these issues, the Buckeye DC was soon overwhelmed by the inventory coming in. Aggravating matters further, as the Washington trucks were unloaded, it became apparent that many of the trucks' inventory counts were inaccurate: trucks were arriving with missing product or completely different product than was on the paperwork included with the shipment. With trucks from Washington constantly flowing in, a quota of unloading at least 10 trucks a day, and inadequate equipment, harried Receiving teams began ignoring the counts of what inventory should have been in the trucks according to NAV, and began manually recording what inventory was actually arriving on paper or via Excel spreadsheet. Since the storage racks were still being built and the prior storage plan based on Oracle was not viable, warehouse workers placed inventory on any available shelf space. When that ran out, they began stacking the inventory on the warehouse floor or in the loading bays. Soon, nearly 50% of the inventory from Washington was "missing" within the warehouse – DC workers responsible for locating product to fulfill orders simply could not find the right product on the shelves via the existing NAV system. Teams would have to do "investigations" – searches to locate missing or misplaced inventory – up to ***50*** times a day in May 2022. By June 2022, as the Washington trucks continued to pour in, the number of investigations per day grew to ***120***.

11. The problems at the Buckeye DC multiplied further when, in June 2022, transocean shipping containers containing inventory that had been stuck in port since 4Q21 or 1Q22 began to arrive along with the Washington trucks. At that point in time, the DC was still unloading the Washington inventory (including all the dead product that had been shipped down to Arizona) and had no available bays to unload the containers and no shelves to put the inventory on. Unloaded shipping containers began piling up, and by the end of July 2022, there were ***three to five hundred*** shipping containers full of rapidly aging inventory sitting in Funko's parking lot. Not only was Funko accruing massive freight rental charges on the containers the longer they sat, but the NAV

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system used by the DC would not show product as "in-stock" and available for shipping until the inventory was physically unloaded into the warehouse. Unable to find missing product from Washington or unload the product they knew was in the shipping containers, pallets of partial orders littered the warehouse floor, unable to be completed and shipped. By August 2022, the DC had a 52-day backlog of orders to ship.

12. Amidst this chaos, on August 4, 2022, Funko issued its financial results for 2Q22 on a Form 8-K filed with the SEC. While its sales numbers had been excellent, and the Company increased its sales guidance for the full year 2022, it did not similarly increase its adjusted EBITDA margin guidance. Defendants also made the announcement that everyone inside Funko had known was coming since Fall Jung first provided an early 3Q22 date for launching Oracle in March 2022 – Oracle was not going to be implemented that quarter, or even that year. Instead, Defendants told investors that they had decided to push the Oracle implementation out to 2023, so as not to disrupt the Company's current "momentum" heading into its important end-of-year holiday sales season. And, while Defendants were now saying that SG&A spend on infrastructure projects would continue into the back half of the year, they reassured investors that the continued expenses would not "present a headwind" and that there were additional "offsetting factors" that would limit any impact on the Company's 2022 financial results.

13. Throughout the earnings call that day, Defendants actively concealed the ongoing problems at the Buckeye DC that were disrupting its order fulfillment – instead misleadingly suggesting that the facility was "up and running" and that the consolidation of the warehouses to the DC was in its final transition stage. Speaking of the Company's dramatically increased inventory levels compared to the second quarter of 2021, Defendants simply attributed the increase to the receipt of delayed inventory, and stated that their inventory was "generally high quality." This, of course, was at best a half-truth: Funko was also sitting on millions of dollars' worth of dead inventory it would never sell, and was accumulating more the longer that product sat in unopened shipping containers.

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14. Following Funko's lackluster 2Q22 guidance and commentary, Funko's Class A stock price declined 18%, closing at $21.81 on August 5, 2022 from a prior day's closing price of $26.69. However, as Defendants had concealed the true extent of Funko's operational foundering, the stock price remained artificially inflated.

15. By September 2022, the situation in the Buckeye DC was intractable. Orders were shipped with only a portion of the ordered product, while retail customers tired of shipping delays or no longer needing the now-outdated product reduced or cancelled their orders entirely. When a Sales account manager for a large retailer asked for an order of Valentines' Day-themed product sitting in one of Funko's hundreds of unopened containers to be unloaded and shipped by October, at the latest, they were told that the earliest the DC would be able to ship the order was ***May 2023 – seven months*** later. Despite Fall Jung telling investors at Funko's September 13, 2022 investor day that the Company would not need additional distribution capabilities for "the next, call it, 12 months or so," by the end of September, Funko had rented an additional third-party warehouse to store its slow-selling and dead inventory so that it could begin unloading product actually needed for orders. Within a few months, it had rented a second. Altogether, the slow-moving and obsolete inventory in Funko's possession took up between 300,000 to 400,000 square feet of warehouse space – equivalent to 1/3 to 1/2 of the entire Buckeye DC.

16. The truth regarding the Buckeye DC's desperate state was revealed on November 3, 2022, when Funko announced its financial results for 3Q22. In addition to accruing a whopping $97.9 million in SG&A costs for the quarter, adjusted earnings per diluted share missed analyst consensus by almost 45%, while inventories were 88.7% higher than at the end of the third quarter of 2021. The Company also lowered its 2022 financial guidance, telling investors to expect a "decline in gross margin due to margin seasonality and ongoing inventory management," and adjusted EBITDA margin of high single digits rather than the previously guided 14.6%. And, just two months out from the end of the year, Funko slashed its 2022 adjusted net income guidance and expected adjusted earnings per diluted share by ***60% each***.

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17. Speaking on the Company's earnings call that day, Perlmutter finally admitted that they had designed the Buckeye DC around Oracle WMS and that the warehouse was not operating efficiently without it. Fall Jung acknowledged that "higher expenses consist[ing] primarily of greater labor costs within the facility and additional machinery to support product movement" had a significant impact on adjusted EBITDA during the quarter. And, far from the 80 bps of increased margin pressure, limited to the first half of the year, that Fall Jung had repeatedly promised investors, she now conceded that the SG&A investment impact on Funko's margin profile would persist at least until the Oracle implementation occurred in summer 2023. Despite all this, Defendants acknowledged that Funko's inventory levels were high but still disclaimed any problem, instead maintaining that the inventory was "generally high quality."

18. Analysts and investors were aghast at these revelations. Said one analyst, "***[i]t feels like we were hit with a bomb***." Another referred to the guidance and commentary as ***"inexplicable"*** and stated that Funko's management now had "***a credibility issue***." Funko's share price dropped an astounding ***59%*** in a single day as artificial inflation from Defendants' fraud was removed, closing at $7.92 per share on November 4, 2022, from a prior day close of $19.50.

19. A few weeks later, Perlmutter was demoted back to his former sales-focused role as President, and Fall Jung was fired.

20. When the Company announced its 4Q22 and fiscal year ("FY22") earnings on March 1, 2023, investors were further disappointed to hear that net income for FY22 had decreased 108% compared to the prior year, while the Company's adjusted earnings per diluted share was just $0.57 – ***32% to 40%*** lower than the already drastically reduced range the Company had guided to in November. On the Company's earnings call that day, new management (former CEO Brian Mariotti stepped back in as CEO with a new CFO, Steve Nave) had additional shocking announcements. First, the Company had decided to abandon the Oracle ERP project completely, taking a ***$32.5 million*** write-down of capitalized costs associated with the years-long project. Second, the Company intended to eliminate and write down ***$30-$36 million*** of Funko inventory

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in the first half of 2023 in order to "manag[e] inventory levels to align with the operating capacity of our distribution center."

21. Following these revelations, Funko's Class A stock price closed at $9.94 on March 2, 2023 from a prior day close of $10.70, as the remaining inflation from Defendants' left Funko's share price.

II. JURISDICTION AND VENUE

22. The claims asserted herein arise under and pursuant to §§10(b) and 20(a) of the Exchange Act, 15 U.S.C. §§78j(b) and 78t(a), and SEC Rule 10b-5, 17 C.F.R. §240.10b-5. This Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. §1331 and §27 of the Exchange Act.

23. Venue is proper in this District pursuant to §27 of the Exchange Act because the Company's principal executive offices are located in this District, and many of the acts and practices complained of herein occurred in this District, including the dissemination of false and misleading statements into this District.

24. In connection with the acts and conduct alleged in this Complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, the mails and interstate wire and telephone communications.

III. PARTIES

A. Plaintiffs

25. Lead Plaintiff Construction Laborers Pension Trust of Greater St. Louis is a multi-employer defined benefit pension plan with approximately $1 billion in assets under management. Construction Laborers Pension Trust of Greater St. Louis purchased shares of Funko Class A common stock during the Class Period at artificially inflated prices and was damaged thereby. *See* Dkt. # 23-2; Dkt. # 23-3.

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26. Plaintiff Paul Haddock also purchased shares of Funko Class A common stock during the Class Period at artificially inflated prices and was damaged thereby. *See* Ex. A, attached hereto.

B. Defendants

27. **Funko, Inc**. is a holding company incorporated under the laws of Delaware on April 21, 2017 in order to complete an initial public offering ("IPO") of Class A common stock and related transactions in order to carry on the business of Funko Acquisition Holdings, LLC ("FAH, LLC") and its subsidiaries. FAH, LLC owns 100% of Funko Holdings LLC ("FHL") and FHL in turn owns 100% of Funko, LLC – Funko's operating entity. Funko, LLC designs and produces consumer products including vinyl figures, apparel and accessories, board games, plush, homewares, vinyl records, posters and digital non-fungible tokens ("NFTs") using licensed pop culture content related to movies, TV shows, video games, musicians and sports teams. Funko's corporate headquarters are located in Everett, Washington. Its Class A common stock trades on the Nasdaq under the symbol "FNKO."

28. As of December 31, 2022, Funko owned 91.6% of FAH, LLC. The remaining interest in FAH, LLC is held (via common units that may be exchanged for Funko Class A shares) by a group of pre-IPO investors and executives, including former CEO Brian Mariotti ("Mariotti"), Perlmutter, ACON Funko Investors, LLC ("ACON"), Fundamental Capital, LLC, and Funko International, LLC (together, the "FAH Holders").

29. On May 5, 2022, Funko announced that an investor consortium led by The Chernin Group ("TCG"), and including eBay Inc., former Disney Chairman and CEO Robert A. Iger, and sports agent and businessman Rich Paul (together, the "TCG Investor Consortium"), would be making a $263 million investment in Funko, acquiring 12,520,559 shares of Funko Class A common stock (80% of ACON Investments' shares in the Company) at $21.00 per share. As a result of the acquisition, which closed on May 19, 2022, TCG owned 25% of the Company and held the right to appoint two directors to the Funko Board. It appointed TCG Co-Founder Jesse

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Jacobs and Rich Paul to the Board, with Robert A. Iger and TCG's Peter Chernin serving as additional advisors to the Company.

30. **Andrew M. Perlmutter** was the CEO of Funko from January 2022 to December 5, 2022, and has been a member of the Board of Directors since January 2022. From October 2017 to January 2022, Perlmutter was Funko's President, focusing on brand development and licensing partnerships, and the Board returned him to that role following the events described herein, in December 2022. Prior to the Company's IPO, Perlmutter was the Senior Vice President of Sales of FAH, LLC from June 2013 to October 2017. As the Company's CEO, Perlmutter was the senior-most officer of the Company, with ultimate responsibility for the Company's operations and performance, and for communicating with the Board. Perlmutter also had approval over Funko's SEC reporting, submitted certifications pursuant to the Sarbanes-Oxley Act of 2002 ("SOX") affirming the accuracy of the financial statements and adequacy of the Company's internal financial controls, and communicated directly with shareholders and market analysts through the Company's earnings calls and other market-related events.

31. **Jennifer Fall Jung** was Funko's CFO from August 2019 until December 5, 2022, when the Board replaced Fall Jung with Interim CFO Scott Yessner following the events described herein. Prior to joining Funko, Fall Jung spent a decade in numerous senior financial executive positions within Gap, Inc., including serving as the Senior Vice President, Corporate Finance and Investor Relations of Gap, Inc., the CFO of Old Navy Global, CFO of Gap North America, and CFO of Gap, Inc. Outlet, where her experience included "e-commerce, capital allocation, logistics and distribution, and inventory management." As the CFO of Funko, Fall Jung was the Company's principal financial officer and principal accounting officer, leading the Company's finance, sales, accounting and Demand Planning, Procurement and Forecasting groups, among others. Fall Jung also had approval over and was signatory to Funko's SEC reporting, submitted SOX certifications affirming the accuracy of the financial statements and adequacy of the Company's internal

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financial controls, and communicated directly with shareholders and market analysts through the Company's earnings calls and other market-related events.

IV. FACTUAL ALLEGATIONS

A. The Company

32. Funko's business is "built on the principle that almost everyone is a fan of something" – whether a TV show, movie, music, or sports team – and the Company designs, sources and distributes vinyl figures and other consumer products around that fandom with licensed content. Major Funko licensors during the Class Period included, *e.g.*, Disney, Marvel, HBO, LucasFilm, Netflix, Pokémon, the National Football League, NBCUniversal, Epic Games, Blizzard Entertainment, and Warner Bros.

33. Funko divides its products into three categories. The first, which accounted for approximately 76% of the Company's sales during FY22, is Core Collectibles. Core Collectibles includes Funko's various pop culture figurine brands: its distinctive Pop! Vinyl figures, and newer collectible brands such as Soda, Vinyl Gold and Popsies.

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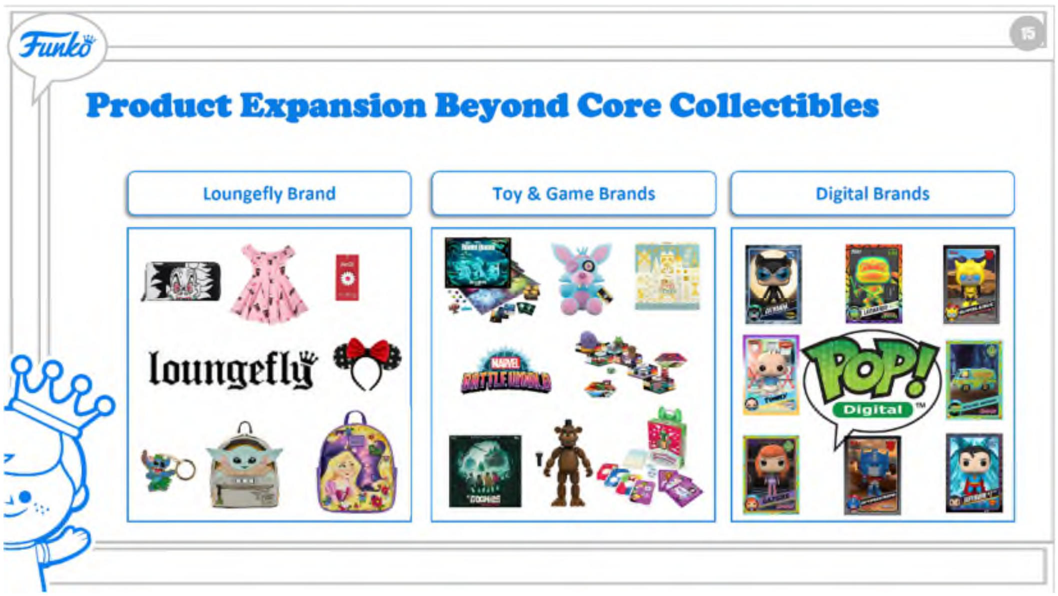
34. The second category, Funko's Loungefly brand, consists of "softline" products – clothing, accessories, bags, wallets and plush toys – and represented 19% of Funko's net sales in 2022. The third category, simply called "Other," includes toys and games and digital content (NFTs), and accounted for approximately 5% of Funko's net sales in 2022.



35. Funko's products are also divided into two categories based on whether they concern "evergreen" pop culture properties – licensed properties based on movies, TV shows, video games, music, sports, or other entertainment content not tied to a new or current release at the time Funko release a product – or "current release" properties – licensed properties based on new movies, current TV shows, or new video game titles. While the evergreen properties, such as Star Wars Classic, Harry Potter, certain DC Comics and Marvel characters, and WWE, do not have a defined duration of market demand, current release properties are intended to "capitalize on the excitement of fans surrounding the launch of new content" and have a limited duration of market demand depending on how popular the content ultimately proves. Accordingly, Funko is given visibility into the new release schedule of many of its license partners and content providers months ahead of time so that it can create new products to time with the release of the new content.

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36. Funko's sales are primarily made through mass-market retailers (*e.g.*, Target, Walmart, and Amazon) and large specialty retailers (*e.g.*, GameStop, Hot Topic, Barnes & Noble), with additional sales made to small or regional stores. During the Class Period, Funko's direct-to-consumer, or "e-Commerce," sales also grew significantly, with the Company putting more priority on the high-margin segment and promoting exclusive Core Collectibles releases on the Funko website. There is also a thriving secondary market for Funko products among the Funko collector community (estimated to comprise about one-third of Funko customers) that takes place through websites like eBay and Facebook Marketplace, as well as through resale vendors at comic book conventions, etc.

B. Funko's Limited-Lifespan Products Made Inventory Control Imperative

37. Funko's extensive licensing portfolio is critical to its business model and by the end of 2021, Funko held over 900 active licenses for characters and other pop culture IP from content providers. During the Class Period, these licenses typically allowed Funko to use the licensed content to design and manufacture Funko products based on the content for two-to-three year periods. In exchange, the licensor received royalty fees based on a percentage of the revenue earned from the Funko product using their IP. Because the license agreements also generally guaranteed minimum royalty payments to the licensor, Funko's revenue from the product needed to surpass the contracted minimum royalty payment in order for the Company to make a profit. License agreements also generally contained terms governing the minimum amount that Funko could charge for the products and what percentage of sales Funko would have to spend on marketing the product.

38. Critically, the contracts also specified that the licensors owned the intellectual property rights in the products Funko designed and sold under the license, such that upon termination of those licenses, Funko no longer had the right to sell those products. Inventory that

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Funko was no longer allowed to sell due to license expirations or older inventory that could not be sold because of a lack of consumer demand was referred to internally as “dead” product.

39. Funko’s need to capitalize on pop culture events and trends, and its limited-life licensing agreements had several important implications for its business.

40. First, to capitalize on its licenses and generally shortlived market demand for current release properties, it was essential that Funko be able to quickly design, manufacture and ship its products. During the Class Period, Funko touted that its production model enabled it to “go from product design of a figure to the store shelf within 110 to 200 days . . . with a minimal upfront investment for most figures of $5,000 to $7,500 in tooling, molds and internal design costs.” However, depending on the licensor and the terms of the license agreement, it could take months for a product design to be negotiated and approved between the licensor and Funko before it could be manufactured. This generally meant that Funko had approximately one year to sell its products before the inventory became “dead.”

41. Second, the limited sales-life of Funko’s products heightened the importance of accurate demand forecasting and inventory management. Funko’s products were both increasingly unlikely to sell the longer they sat on shelves, and at a certain point, unable to be sold at all. Unsellable inventory (or slow-moving inventory only sellable at a steep discount) not only cost the Company in terms of manufacturing and freight from its China or Vietnam factories to its distribution centers, but also because it had to be stored, occupying valuable warehouse space needed for new products. (Dead products were eventually sent to a landfill or recycled via a third-party disposal service.) More, Funko based its financial projections in part on sales of those products; the lost revenue from undesirable product could cause the Company to miss financial targets it had established for Wall Street and investors.

42. Funko experienced these exact problems in 2019, when it accumulated more than ***10 to 12 million*** obsolete units of product in its Everett, Washington warehouses. The unsellable inventory clogged up its warehouses so badly that at one point, Funko had hundreds of shipping

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containers of new product it could not unload sitting in its parking lot and the Port of Seattle. Rather than get rid of the inventory, the Company eventually leased a new warehouse in Puyallup, Washington, to continue storing it. But that was simply putting a Band-Aid on a bullet hole, and on February 5, 2020, Funko publicly announced it needed to write down $16.8 million in inventory "to dispose of slower moving inventory to increase operational capacity." Funko's share price decreased 40% in a single day following the news.

43. Perlmutter and Fall Jung were Funko's President and CFO, respectively, at the time of the 2020 write-down and stock price drop and, as a result, well understood what would happen if the Company's inventory management was not done properly in the future. Inventory needs and availability were discussed in at least monthly Sales Operations meetings attended by Perlmutter, Fall Jung, senior leaders and key account managers from the Sales and Operations Planning ("S&OP") group (which reported to Fall Jung), and Sales team (which Perlmutter was heavily involved in), and from Chief Operating Officer ("COO") Joe Sansone's Fulfillment Operations group. The Vice President of Sales would request a particular amount of inventory be ordered based on Sales team demand forecasts for the upcoming quarters, ostensibly based on prior year sales and projected growth.

44. However, according to a former Business Planner who worked for the Company's S&OP group from 2020 through at least 1Q22, the demand numbers provided by Sales were unrealistically optimistic given the evident sales growth slowdown following an unprecedented collectibles boom during the COVID-19 pandemic. The S&OP forecasts showed significantly lower growth in demand post-COVID-19. But although S&OP was intended to serve as a "gatekeeper" to verify Sales' demand numbers, it was widely known within the S&OP team that Funko's senior management was unwilling to accept that Funko might not continue to grow at the same rapid pace as it did during COVID-19 pandemic. The Company always adopted the Sales team's forecasts, and there were no effective controls in place to curb the excess inventory purchasing.

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45. The Company was able to track inventory through a number of computer systems, including via Microsoft NAV. Reports were circulated among the Sales teams and at Sales Operations meetings showing what product was currently available for sale and when that product had been released. Funko also had data from their major retail clients as to what product had been sold from the stores' shelves, so they could see what was popular and what product wasn't moving. The Company also had detailed tracking information about the status of their product as it was shipped from the factories, and knew where the transocean shipping containers were and when the inventory would be due to arrive at Funko's distribution centers. The Sales team would discuss the products that weren't selling at the regular meetings, and would use the information on available, upcoming and trending products to come up with pitches for major retailers as to what product they should put on their Funko-allocated store shelf-space next. Ultimately, Funko's largest accounts – Amazon, Walmart, Target, and other "big box" stores – wanted to buy new Funko products, not reorder aging product Funko might still have in its inventory.

46. Funko's risk of overbuying inventory was further exacerbated by its policy, in place until September 2022, of allowing retail customers to cancel or modify their orders up until the time the orders shipped from Funko's warehouse without penalty. For example, in 2021, Funko had a license to make FunkoPop!s of approximately a dozen movie characters from a Marvel movie that was anticipated to be a big hit, Eternals. But when the movie was released in November 2021, it was not popular with the public – certainly, it was not so popular that fans would eagerly snatch up FunkoPop!s of all of the characters. Seeing the writing on the wall, Funko retailers cancelled or substantially reduced their original orders of Eternals products. As a result, in 2022, Funko had huge amounts of unsold Eternals inventory sitting in its Washington warehouses that it knew it would never sell.

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C. Funko's Plans to Upgrade Its Inadequate Infrastructure During the Class Period

47. The Company knew that it could not continue to grow without undertaking some major infrastructure projects to support that growth. First among the needed upgrades was replacing the Company's ERP software. The system that the Company had been using across its processes and in its warehouses, Microsoft NAV, was antiquated, designed for small- to mid-sized companies, and no longer able to handle the workload that the Company was putting on it. Not only was the system in its current state underpowered, but employees frustrated with its functionality often had to use manual workarounds to get the analytics and data they wanted. The S&OP team, for example, often used Excel spreadsheets for their analytics rather than use Microsoft NAV. A more powerful system was needed that could integrate the data from all of the Company's various functions (*e.g.*, accounting and finance, supply chain, demand planning, inventory management, sales) as well as those of its acquired companies (Loungefly, and later, Mondo) and provide the analytic tools necessary to ensure the Company's operations could be run efficiently and its financial information tracked reliably. In 2020, the Company decided to go with Oracle as its new ERP system.

48. Defendants understood that transferring the Company's systems and databases from its current system to Oracle was a massive endeavor, and hired several third-party contractors (the lead contractor being IT consulting firm Infosys) to assist Funko with the implementation. Later, smaller pieces of the Oracle implementation were allotted to other firms: Inspirage, Redwood, and Logistics, which designed the portion of the system that would work with parcel companies like FedEx and UPS. After little progress had been made on the project by the end of 2020, in February 2021, Funko hired an ERP Program Manager to serve as a liaison between the Company and Infosys and to oversee the resources assigned to the implementation program. While the project was originally under the direction of Vice President of Technology David Horner, who reported to Sansone, in spring 2021, Sansone took over the project himself.

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D. The Oracle Project Highlights Serious Flaws in Funko's Operations

49. By early 2022, the Oracle project had highlighted numerous, deep-rooted flaws in Funko's operations.

50. In order for Oracle to be effective, Funko needed to "clean" the Company's existing data so that it could be transferred to Oracle properly. This meant Company employees needed to ensure each line of data was accurate, complete, in the right format, and categorized in an appropriate way under Oracle's rules such that it would be captured and usable in the new system. This was an extensive job. For example, the Company's S&OP group's business analytics system required up to 80 points of data for Oracle to operate correctly with respect to just a ***single*** product, or "SKU." That meant that someone on the S&OP team with the requisite institutional knowledge of what information was needed would have to manually go through each point of data for each SKU to ensure it was correct before it could be transferred.

51. This would be a manually intensive process even in a company with generally clean data – and Funko's data was a mess. The Company did not have any data governance – *i.e.*, controls and processes for who creates certain data and how it should be entered into the system – so even the data within a certain function or business line was inconsistent and often incomplete. The employee responsible for conforming the financial data of one of the Company's business units for transfer repeatedly voiced concerns to VP of Merchandising, Planning and Procurement Mike Smith and Manager of Merchandise Financial Planning, Ben Kaestner, about the Company's lack of data governance controls during team meetings to discuss the Oracle project, with no resulting action taken.

52. Funko also wasn't dedicating the necessary organizational resources – nor did management have the necessary experience in ERP system implementation – to ensure that the Oracle integration was done correctly, or that the data transfer would be timely completed. For example, although Funko wanted "New Product Introduction" to be a process included in Oracle,

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it did not assign anyone to oversee the conversion of data related to and needed for that process into the system.

E. Corporate Infighting Hinders Progress

53. Perhaps most problematically, the Oracle project was hindered by deep rifts among Funko senior leadership, which was dysfunctional and indecisive, with constant infighting among key leaders and significant turnover among senior personnel. (For example, within January 2022 alone, S&OP was led by three different people, as Smith, Kaestner, and then Kaestner's replacement each quit.) For the Oracle project to succeed, Funko leadership needed to work together to make decisions as to how the system should be set up, including what business processes should be included in the Oracle integration and how they wanted those processes to function before the system architecture could be designed and implemented. The C-Suite simply could not get "aligned" as to these critical systems architecture decisions, despite bi-weekly "Steering Committee" leadership meetings with all of the C-Suite individuals involved. Fall Jung and Sansone in particular were "oil and water" and constantly at odds with one another at these meetings.

54. By early 2022, it was clear to employees across the Company's various departments that the Oracle project was far from being able to launch by the Company's targeted 2Q22 deadline. The employee cleaning one business unit's financial data told Fall Jung in January or February 2022 during a one-on-one video call that the employee could not see the Oracle program being completed on time and that the project was not going well. IT systems and logistics employees in Funko's U.K. office, which worked with the U.S. office on designing the global Oracle plan reported that in early 2022, it was "quite clear" the project was "not in a good place" and that basic decisions regarding how the Oracle system was going to operate, and who would even be in charge of maintaining the system once it was implemented, had still not even been discussed. As of January 2022, senior IT management did not have a timeline they could provide employees for when the project would realistically be able to go live.

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F. Funko Plans an Upgraded Distribution Center to Enhance Efficiency and Scale

55. The Oracle project was critical to Funko's other major infrastructure project: Funko's consolidation and relocation of its five Washington distribution facilities to one state-of-the-art fulfillment and distribution center that operated on Oracle WMS.

56. The Company's U.K. office had successfully opened a new, state-of-the-art distribution center operating on a different WMS in 2020. The 349,000 square foot distribution center took 15 months to design and complete.

57. Funko's consolidated distribution center in the U.S. would dwarf the recently completed facility in the U.K., as well as its largest operating warehouse in the U.S. (approximately 200,000 square feet). In September 2021, Funko entered into a lease agreement for a mammoth ***860,000*** square foot warehouse and distribution center in Buckeye, Arizona. Buckeye was chosen for Arizona's lower labor costs, its proximity to Long Beach, California's shipping ports, and the fact that there were other large retail operations with distribution centers nearby (Five Below's distribution center was right next door), theoretically providing a pool of experienced applicants to the new Funko DC.

58. Funko's Operations group and Finance group were both involved in planning the new DC, with the Finance group's demand planners providing information on anticipated sales and how much product the warehouse would need to store. The new DC would be run by Senior Director of Fulfillment Operations Dave Tarnosky (who, in turn, reported to VP of Operations Alex Poole and COO Joe Sansone). The DC would have state-of-the-art technology and equipment and include an entire building devoted just to distribution of orders from Funko's growing e-Commerce (direct-to-consumer) business, led by Tarnosky direct-report Rich Schacht. That building would not only house e-Commerce product, it would have specialized high-tech equipment, including a maze-like conveyor belt system, designed for Oracle, that would run

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through the warehouse (enhancing the efficiency of selecting product for and shipping numerous small orders).

59. The Oracle WMS would be essential in enabling workers to efficiently navigate the behemoth new DC and to obtaining the benefits of scale that Funko's anticipated growth required. The Oracle WMS would: (i) allow the DC's Receiving team to scan inventory from trucks as new product came in, confirm that the correct products had been received and that none were missing from the incoming trailers or transocean shipping containers, and identify where in the facility to unload it; (ii) enable workers fulfilling orders ("Pickers") to find where a particular product was housed in the facility and who had put it there so they could "pick" the product for the order or correct product misplacements quickly; and (iii) allow the Freight team to pack and track large retail orders as they were fulfilled.

60. Throughout 2021, Continuous Improvement Manager Chris Chromy held meetings with warehouse Supervisors, Managers, as well as Funko leadership (such as Tarnosky and Poole) to discuss how Oracle should and would be implemented at the new DC. Warehouse management also met with the Oracle implementation team to discuss the specifics of fulfillment and distribution operations so that the business processes and functionality that the DC needed could be integrated into the new system. The discussions included broader process-related issues as well as details such as how long it took workers to unload a truck. The Oracle implementation team provided numerous iterations of Oracle test modules for the DC during 2021, but each time, the programs did not meet warehouse needs or were otherwise non-functional. Meetings between warehouse management and the Oracle integration team stopped before the end of 2021, with no resolution to the Oracle module issues.

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G. Defendants Fraudulently Conceal Struggling Operations from Investors Throughout the Class Period

1. The Class Period Begins

61. The Class Period begins on March 3, 2022. On that day, Funko filed a Form 8-K and Form 10-K for the year ended December 31, 2021 ("FY21") with the SEC and held an earnings call discussing financial results for 4Q21 and FY21 and providing financial guidance for 2022. Defendants touted not only Funko's exceptional revenue growth over the past year, but provided FY22 guidance that far exceeded analyst expectations: adjusted earnings per diluted share of $1.75-$1.91 (versus analyst consensus of $1.39), with adjusted EBITDA margin flat at 14.6% despite higher-than-normal SG&A expense[3] due to the Oracle implementation and Buckeye DC opening during the first half of the year. Perlmutter, on his first earnings call since being promoted to Funko's CEO in January 2022, emphasized that Funko had "proven our ability to deliver in difficult environments, and I'm very confident we are well positioned to meet our objectives for the full year."

62. Speaking to the Company's inventory levels, Fall Jung stated that "[i]nventory at quarter end totaled $162 million, down sequentially from last quarter, but still reflecting an elevated rate of inventory in transit at 40% as transaction freight times remain[] well above pre-pandemic durations."

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[3] SG&A expenses at Funko were:

> primarily driven by wages, commissions and benefits, warehouse, fulfillment (internal and external), rent and facilities costs, infrastructure and technology costs, advertising and marketing expenses, including the costs to participate at specialty licensing and comic book conventions and exhibitions, as well as costs to develop promotional video and other online content created for advertising purposes. Credit card fees, insurance, legal expenses, other professional expenses and other miscellaneous operating costs are also included in selling, general and administrative expenses.

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63. Providing an update on the ERP and Buckeye DC projects, Fall Jung stated that "SG&A as a percent of sales is also expected to be slightly higher in the first half of the year due to the timing of project costs associated with the consolidation and relocation of our distribution center as well as our ERP implementation." Jefferies, LLC ("Jefferies") followed up on the statement later in the call, asking Fall Jung: "You gave 80 basis points of pressure from – it seems like more of a transitory DC and ERP implementation and transition. Any context on when that 80 basis points is concentrated? Is it first half, second half? Anything we should be mindful of?" Fall Jung affirmed: "Yes, Yes, ***first half for sure***. [W]e will probably launch in the beginning early [sic] the Q3 for the ERP, but the distribution center move will happen in the first half."

64. Internally, however, it was clear that the Company's infrastructure projects were nowhere close to being completed (or their costs accrued) by the deadlines Fall Jung promised so affirmatively. Numerous employees involved with the Oracle project stated that by January 2022, it was evident inside the Company that the ERP would not be operative by July or August 2022 (*i.e.*, the first two months of 3Q22). They did not know why Fall Jung would have stated that it ***could*** be live by that time, particularly since the C-Suite received regular status reports discussing the ongoing problems that needed to be dealt with (but weren't being dealt with) prior to the project's implementation.

65. More, Funko's lease for the Buckeye DC allowed them to occupy the space on April 1, 2022, and when they moved in, it would be a largely blank canvas. Funko would have to build bathrooms, offices for warehouse management, not to mention the storage racks and equipment installation necessary for a functional distribution center. There were nowhere near enough employees transferring from Funko's Washington warehouses to fully staff the huge Buckeye DC (it was anticipated to require 300 more workers, at least), and Funko hadn't done any of the needed hiring yet. In fact, the plan was for warehouse workers to be hired in "waves" so that the experienced Washington supervisors could train the new Buckeye DC hires appropriately.

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And, as explained above, the Oracle WMS – ***the system that the entire DC was planned around*** – would not be available.

2. April-May 2022: The Buckeye DC Is Wholly Unprepared for and Overwhelmed by the Inventory Sent from Washington

66. On April 4, 2022, the warehouse "opened" for warehouse management who had moved from Washington to come for their first day of work, to tour the warehouse space and make plans for training new employees. There were no offices, and the Company was operating the DC under a temporary certificate of occupancy, with necessary building work – like installation of the storage racks that Funko's product would be placed on (each of which had to be inspected and permitted by the local government building office), and equipping loading bays to receive product – ***months*** from being completed.

67. By the time new employee training started in late April, the Company had not yet finished building out the space. Other problems with the DC were also apparent. The corporate team responsible for ordering warehouse equipment had not spoken to warehouse management before ordering, and the equipment was not adequate for worker needs. For example, the Company had purchased "extendo" conveyor belt systems that hooked up to the backs of trailers to help load and unload them. But the systems they purchased were too tall for most employees to be able to lift boxes on and off the belts to load the trucks. The need to work around equipment, rather than with it, caused extensive delays and decreased DC productivity. Similarly, despite the fact that the massive warehouse had been designed to have at least eight levels of vertical shelving, the warehouse only had one "E-Pick" reach truck that was capable of reaching the top three levels.

68. Additionally, the Company had so much inventory in its Washington warehouses that it would take ***three months*** to truck it all to Arizona utilizing rented trucks and trailers. At the beginning of 2022, each of Funko's five Washington warehouses and distribution centers was operating roughly at capacity. The plan was to stagger the inventory's arrival: first, retail inventory would be sent, then e-Commerce product. Loungefly inventory, which had always been stored

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and shipped via a third-party logistics company, would continue to be stored and shipped via third-party services. Trucks began arriving in Buckeye with inventory from the Washington warehouses in late April, despite the fact that only a fraction of the loading bays (12 of the planned 84) were operable for Receiving and racks were still under construction.

69. The Receiving department was given a quota of receiving, unloading and putting away 10 trailer loads of inventory per day, around 20,000 units of product.[4] Since the trailers were rented, they would continue to rack up charges the longer they sat and waited to be unloaded – Funko needed them unloaded promptly to avoid incurring more cost.

70. Foreseeably, the DC was wholly unprepared for the onslaught of inventory. The warehouse workers on the Receiving team, some new hires to Funko and others temporary employees sent by an outside agency, had not yet received their training, and there were no usable SOPs describing how the Receiving process was supposed to work at the Buckeye warehouse.[5] One former warehouse employee recalled going to the DC in early April for an interview and a tour of the distribution center, and he and other prospective employees seeing several trucks containing Funko product pull up to the building. The DC employees giving the tour asked the prospective employees if they would be willing to start working immediately, quickly certified the group to operate the machinery, and told the group to start putting the product they were unloading on any open racks in the warehouse. ***None*** of the product was scanned in electronically so that its location would be tracked within the enormous DC. A former Operations Lead at one of Funko's Washington warehouses who was sent to Buckeye in May 2022 to train new DC employees repeatedly witnessed the Receiving team unload inventory from the Washington warehouses without reviewing the associated shipping documentation and double-checking inventory counts,

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[4] Trailers were 53 feet long, holding approximately 30 pallets of product each (each pallet holding approximately 700 standard sized FunkoPop!s).

[5] Funko had SOPs for Buckeye that were written with the assumption that Oracle was live and usable; with Oracle not operational, the SOPs were worthless.

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a problem the horrified Operations Lead told DC management would "come back to haunt" the Company if not fixed quickly (it was not, and did).

71. Further, when workers did review the shipping documentation for the trucks coming in from the Washington warehouses, it was apparent that employees loading the trucks had bungled the transfer paperwork – trailers were missing product, had extra product, or contained entirely different product than what was supposed to be in the delivery. Eventually, someone directed the workers receiving product at the Buckeye DC to update the NAV system with the number of products the DC actually received, changing important inventory counts in the Company's system. (Because NAV did not limit user permissions to be able to change these counts, and new hires' NAV credentials were created by mirroring the permissions of other workers' accounts, most workers could do so.) When a new shipping container came in, there was no way to confirm that the product received was the same product that was supposed to be in the container, making inventory tracking nearly impossible. One former Operations Lead recalled having to deal with "50 investigations" per day while in Buckeye – instances in which an employee identified that specific inventory wasn't located where it was supposed to be in the DC, and the team would have to track it down.

72. The former Operations Lead was so concerned by what they saw at Buckeye that they wrote a heated letter to an Operations Manager at Funko. The letter described the ways in which warehouse supervisors were not following correct receiving/inventory processes. When the former employee returned to Everett after two weeks in Buckeye, Tarnosky interviewed the employee about the contents of the letter in person, seeming to agree with its contents.

73. At bottom, the fact that the warehouse had been designed to utilize Oracle, but was instead operating on Microsoft NAV, was causing major disruption. The Receiving process written for Oracle would have had the Receiving team: scan incoming inventory when it was unloaded, view in Oracle which shelf the inventory was designated to put it on, put the inventory on the shelf, and then scan that location so that the inventory was registered at the location and it

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was recorded who specifically handled it. NAV was not nearly as precise – not to mention that the lack of equipment within the DC meant that a majority of the handheld scanners at the warehouse were used by the Pickers and frequently not available to Receiving during the first month.

74. The antiquated NAV system simply couldn't handle the workload of the new consolidated warehouse, and Buckeye DC workers frequently experienced system errors and problems getting updated information from the system. The issues on Microsoft NAV became so problematic that DC workers began using Excel spreadsheets or even written notes to account for shipments, rather than doing so in NAV. Notably, the Company had made no effort to train any of the DC employees on the Oracle system purportedly set to go live in early 3Q22, at any point in the first half of 2022, nor was training new employees on the Oracle WMS discussed.

75. Within a month of the DC opening, there were no more available racks for the Receiving team to use when unloading the truck trailers from Washington. When that happened, product was stacked in a large rectangular area of warehouse floor without any particular organization or identification. Pickers trying to locate product for order fulfillment had no idea where to locate items – NAV would simply direct them to a general area of the warehouse where boxes of unknown product were stacked haphazardly. Because it could take hours to fulfill a single order if product was in that "lost" area, and because the Company generally did not ship orders until all or at least a significant portion of items in the order were in stock, order fulfillment began to get backed up. Pallets of partial orders waiting to be completed littered the floor. An Operations Manager at Buckeye estimates that approximately 50% of the Washington inventory was misplaced, its location unknown within the warehouse.

76. Compounding the lack of storage, senior management, including VP of Operations Alex Poole (who reported to Sansone), had decided to ship all of the "dead" inventory in the Washington warehouses to Buckeye rather than dispose of it. And there was a ***lot*** of dead inventory – according to a Supervisor in EV1, the Company's largest warehouse, approximately ***25%*** of the

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warehoused product in EV1 was dead inventory at the beginning of 2022. Employees could determine product was dead by looking at the Company's various computer systems (including NAV) to see when it had been released or last been sold, and it was obvious to any casual observer which warehoused product was dead as well – boxes were caked in dust and clearly had not been moved in years.

77. Another warehouse Supervisor and longtime Funko employee, who worked at the Company throughout the entire Class Period confirmed that each of the five warehouses contained dead inventory mixed in the shelves among the selling product, although most was located in EV1. Up until 2020, the Company's headquarters had periodically provided a list of dead inventory with instructions for the warehouses to send it to third-party disposal service Green Planet to be destroyed and recycled (to the extent possible). However, when COVID-19 hit and Funko's sales shot up rapidly, Company management and warehouse workers were focused on achieving maximum sales and fulfilling the orders coming in, respectively, rather than managing the dead inventory.

78. Accordingly, by the time the inventory was being shipped to Buckeye in spring 2022, the Company had not destroyed any dead inventory in ***two years*** – during which time Funko had experienced pandemic-related shipping delays, delayed movie releases that had impacted product sales, the Eternals flop, and other significant events that increased the amount of dead inventory on hand. One warehouse Supervisor estimated that approximately 30% of the Washington inventory received at Buckeye in spring 2022 was already dead. Another recalls discussing the decision not to deal with the dead inventory with Tarnosky and his direct report, Assistant General Manager John Mora, in early 2022, and being told "[t]he decision was made and communicated down that we are just going to send it all and sort it when we get there." That decision not only cost Funko hundreds of thousands of dollars in shipping, but also clogged up Buckeye's operations: unsellable product needed to be unloaded and stored, taking up man-hours,

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unloading equipment (a scarce resource at Buckeye) and rack space badly needed for inventory that had actually been ordered by customers.

3. While the Buckeye DC Founders, Defendants Maintain Their Misleading Infrastructure and Costs Timeline and Conceal Accumulating Dead Inventory

79. On May 5, 2022, as the Buckeye DC was struggling to get operations underway, Funko filed a Form 8-K with the SEC announcing its financial results for 1Q22. Among the figures reported was that Funko's inventories at the end of 1Q22 totaled $161.5 million, up 160.8% over the prior year. According to the release, "[r]eported inventory includes in-transit inventory, which comprised 40% of total inventory, reflecting a significant increase in trans-ocean times due to pandemic-related supply chain disruptions." The release also provided updated FY22 financial guidance, raising its net sales guidance and maintaining that adjusted EBITDA margin would be approximately 14.6%, reflecting "approximately 80 bps of headwind from one-time project spend associated with the consolidation and relocation of our U.S.-based distribution center and the implementation of our new ERP system."

80. On the Company's earnings call later that day, Fall Jung once again reiterated that Funko "remain[ed] on track to reach our full year adjusted EBITDA target of a margin consistent with 2021 results," and that the target "reflects the ongoing freight inflation headwinds as well as approximately 80 basis points of pressure due to onetime project spend from the consolidation and relocation of our distribution centers and the implementation of our ERP system." Asked by an analyst about the project spend for the ERP and DC, specifically how much the Company anticipated spending and in what quarters, Fall Jung affirmed, "***yes, we reported out that was about 80 basis points on the year, all of which will happen in the first half of the year***. It's about 2 points of pressure just in Q2 on adjusted EBITDA. So we're launching – or ***we did launch the new DC in April, and the ERP is set to come out at the end of the quarter. . . . It's really the pressures [sic] all in the first half of the year, specifically Q2***."

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81. According to numerous former Funko employees involved in the Oracle project, the Company was certainly not going to launch its ERP by the end of June. The warehouse Supervisor who worked on the project with Funko IT and the Oracle implementation team stated that he had listened to the 2Q22 earnings call, and thought Fall Jung's statement "was a weird thing to say, [we] were definitely not going to have it online" by the end of 2Q22. He and other warehouse Supervisors hadn't heard any mention of Oracle implementation, let alone been trained on Oracle, by the time of the 1Q22 earnings call.

82. Analysts reporting on the Company, however, took Fall Jung's representation that the additional SG&A costs would be limited to 1H22 at face value. Jefferies noted in its May 5, 2022 report that "SG&A % takes a 100bps quarterly step-up in Q2 for ERP implementation timing & DC relocation, followed by normalization in 2H22." D.A. Davidson & Co.'s ("D.A. Davidson") May 6, 2022 report stated that: "The vast majority of the one-time project spending will occur in 2Q22, with an impact on EBITDA margin of ~200bp. Gross margin is expected to be down sequentially in 2Q22 due to the timing of certain items, and the SG&A expense ratio will be up sequentially due to the one-time spending, which should be complete by the end of 2Q22."

83. Later, a May 2022 Funko investor presentation misleadingly touted the ways in which Funko was increasing operational efficiency, including by "Investing in Domestic ERP" and "Optimizing Inventory Levels"[6] – glossing over the fact that, as Defendants knew, ***neither*** infrastructure project was in fact increasing Funko's operational efficiency.

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[6] *Available at* https://s24.q4cdn.com/627994544/files/Funko-Investor-Presentation-2022.05.10.pdf (last accessed October 2, 2023).

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4. The Buckeye DC Drowns in Inventory Throughout Summer 2022, Limiting Funko's Distribution Capabilities

84. By June, the chaos at the Buckeye warehouse had only increased. VP of Operations Alex Poole, who had been largely responsible for the Buckeye warehouse, quit. Soon after, COO Sansone began appearing at Buckeye regularly, spending at least one or two weeks per month at the warehouse, having meetings with Tarnosky and Mora about the DC and walking the floor speaking with warehouse employees trying to solve immediate problems. Employees wanting to train on the Oracle ERP system they had been told by Funko's Human Resources group that the warehouse was eventually going to run on before they were hired were told that training on the system was not happening. There still were no SOPs for the various roles in the warehouse, and Funko was realizing it had hired too many people for certain roles, and too few in others. As a result, few of the new Buckeye employees that had been hired knew what they were supposed to be doing and entire shifts of individuals ended up with nothing to do except sweep the warehouse

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floors.[7] The DC was still being built out (though the Company finally received a permanent certificate of occupancy in June), and they still were in desperate need of additional equipment (by June, the DC had acquired two more high-reach "E-Pick" machines, for a grand total of three). Racks were filled as soon as they were usable, with the DC regularly operating at over 95% capacity. Rented trailers of inventory from the Washington warehouses were still steadily arriving, being unloaded, and with no Oracle system to assist with keeping track of inventory placement, manually checked into storage at the warehouse or misplaced. The number of needed daily "investigations" into missing or misplaced inventory grew as high as ***120*** per day.

85. The chaos increased exponentially at the end of the month, when shipping containers that had been held up in transit during the COVID-19-related freight slowdowns and port delays in 4Q21 and 1Q22 finally started to arrive with additional inventory. By July 2022, the containers were arriving en masse, along with the remaining trailers from Washington. But the existing racks in the Buckeye DC were already full (including with a substantial amount of non-moving and dead inventory), and while more were still being constructed, workers already had problems finding storage for the remaining Washington inventory. The ocean containers coming in had no place to go but the parking lot until there was space for them to be unloaded. Not only was this a problem in terms of logistics, but it was expensive – the containers were rented, freight rates were exceptionally high due to the ongoing shortage of shipping containers, and Funko continued accruing rental charges and late penalties the longer the containers sat unloaded. Throughout 3Q22, Funko had between ***300 and 500*** unloaded containers of product sitting outside the warehouse on any given day.

86. On August 4, 2022, four months after Buckeye opened, Funko filed a Form 8-K announcing its financial results from 2Q22. Gross margin had decreased from 1Q22 by 260 basis points, while SG&A expenses increased to $82.7 million, or 26.2% of net sales, "reflecting higher

[7] The DC was essentially a 24-hour operation on the weekends, with two 12-hour shifts, while during the week there were two 10-hour shifts.

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costs in the second quarter related to the relocation and consolidation of our distribution centers, ERP implementation-related expenses" as promised. Inventories at the end of 2Q22 totaled $234.0 million, up 170.9% compared to a year earlier, and $***72.5 million*** higher than at the end of 1Q22. The Company attributed the increase to "***receipt of delayed inventory*** as pandemic-related supply chain disruptions began to improve towards the end of the quarter" – omitting any mention of the millions of dollars of unsellable inventory now sitting in the Buckeye warehouse, or that the delayed inventory had just months to be sold before it too would be considered dead. Despite its snowballing SG&A costs and inability to make sales due to clogged distribution channels, the Company raised its 2022 net income guidance for the second quarter in a row, and once again maintained it would meet an adjusted EBITDA margin of approximately 14.6% (despite its significant margin decrease in the first half of the year), with adjusted earnings per diluted share of $1.88 to $1.99.

87. The Company's 2Q22 Form 10-Q, also filed on August 4, 2022, disclosed for the first time that the Company "expect[ed] personnel and related costs to remain elevated through at least the end of 2022 to support the final transitions of our U.S. distribution warehouses, additional personnel to support strategic initiatives and overall business growth and due to additional inflationary pressures to increase wages, commissions and benefits expenses," and "also expect[ed] elevated costs related to our enterprise resource planning ('ERP') implementation as we expect to finalize the remaining steps in early 2023" – misleadingly minimizing the havoc at the DC by claiming the Company was just in the "final transition[]" stage, and continuing to conceal that the ERP implementation had been critical to the Buckeye DC's ability to operate.

88. On the 2Q22 earnings call later that day, Fall Jung clarified that Funko had "recently made the difficult decision to delay" its ERP implementation until 2023, because "ultimately, we did not want to impair the momentum that we have today by shifting to a platform that we felt wasn't yet fully ready to support our business." When an analyst asked her whether

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pushing out Funko's ERP initiative meant that there would be less SG&A costs associated with the ERP in 2022, Fall Jung misleadingly downplayed the SG&A costs remaining in 2022, saying,

> No . . . the run rate will continue. But there's other offsetting factors to that. ***So we don't see it as a major headwind in 2022 so far***, but we feel good we made the right decision for the business to not have business interruption as we go into the holiday season.

Asked about whether 2022 would end with lower cash flow than 2021, Fall Jung once again misleadingly implied that the spend in 1H22 on the Buckeye DC had sufficed and it was now fully operational: "What you're seeing underneath the covers there is a couple high unit [sic] of cash . . . ***the distribution center, that was a major feat to get that up and running***."

89. Regarding inventory, Fall Jung omitted mention of the problems caused by the dead inventory clogging up Buckeye or the amount of aged inventory sitting in its parking lot, instead representing that "[w]hile our inventory levels are up year-over-year, we believe that inventory is ***generally high quality*** and leave[s] us well positioned to meet our consumer demand and support our strong second half growth forecast." Asked about "where the inventory resides, how much of it is related to the DC relocation," Fall Jung claimed that "in Q4 [we] had a lot of delays that rolled into Q1 just due to the congestion within the supply chain. And you're seeing a little bit of that in Q2 as well. . . . So there is a large portion of the in-transit, but we're working to get that into the DC and get that out to our customers."

90. Following the August 4, 2022 earnings call, Funko's Class A share price declined by $4.88, or approximately 18%, dropping from a closing price of $26.69 on August 4, 2022, to close at $21.81 on August 5, 2022. Analyst commentary was surprised that guidance did not increase given the better-than-expected 2Q22 sales, but accepted management's representations that they were simply being "conservative" about retail demand in the second half of 2022.

91. By September 2022, Funko's lack of order fulfillment capabilities was impacting its forward sales. Sales team members were given sales quotas that they were supposed to hit for certain periods that were simply impossible for most team members to meet due to missing product

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and artificial product shortages arising from the inability to unload containers. The NAV system used at the warehouse would not show product as in stock and available for "picking" unless it had been physically unloaded in the warehouse – product in the containers wouldn't be registered as in stock. By August 2022, the DC was already more than 50 days behind in fulfilling backlogged orders, and 3Q22 and early 4Q22 were generally when retailers ordered ***and expected shipment of*** their holiday stock.

92. Although logistics planners in Everett and Buckeye tried to coordinate plans to determine which containers were "hot" for the day – *i.e.*, which needed to be prioritized either for a specific order or because the shipping containers were getting too expensive or the product it contained was aging out of being sellable – the DC could not keep up with Sales team needs. There was a constant battle between warehouse departments to use the high reach E-Pick machines, leading to long periods of downtime for those teams that needed to, but couldn't, reach product on the top shelves. The promised conveyor belt system for the e-Commerce building had been designed to be used with Oracle, under constant construction since the warehouse opened and had never been used, meaning that Pickers in that department had to trek across the warehouse to locate any individual's order and get it to the shipping department – a time-consuming and highly inefficient process given the size of the massive building. (The expensive conveyor belt would ultimately be abandoned in 4Q22, being used only a handful of times before it was deemed unusable for its purpose without Oracle.) And, with the DC more than 95% filled at any given time, and overflow inventory being stored on the floors and loading bays, it was difficult for employees to move around, let alone locate and ship pallets of product efficiently.

93. Orders started to be shipped while only partially fulfilled, with in-stock inventory allocated among the various key accounts that had ordered it. Some retail customers cancelled orders altogether, since their shipments were so delayed the product was no longer considered "new" or it would not arrive by the needed point in time, while other retailers only wanted the product if they could obtain a certain quantity. The backlog was so intractable that in one instance

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an Account Manager for a large specialty retailer needed a large amount of Valentine's Day product unloaded and shipped by October 2022 at the latest, and was told that the earliest the DC could get the product out was May 2023, ***seven months*** later. Unsurprisingly, that customer cancelled their order. Funko's new Vice President of Operations, Justin Serfass, routinely reminded DC supervisors that Buckeye's problems stemmed from Funko's poor forecasting and resultant over-ordering of product, and its failure to get an ERP system in place, and that the DC just had to do the best it could.

94. Amidst this chaos, on September 13, 2022, Defendants held a Funko investor day, laying out their strategy for successful growth and their plan to hit a 20% adjusted EBITDA margin by 2026. Fall Jung expressed her confidence in their ability to hit the adjusted EBITDA margin target, saying "[w]e know we're going to get to 20% adjusted EBITDA over the course of this time," and that a major reason for that confidence was the Company's ability to obtain improved operating cost and leverage. According to Fall Jung, the Company's new DC would streamline their logistics, and getting the ERP up and running in 2023 would provide increased operational efficiencies. Asked about future investment needed for the internal growth Funko planned, Fall Jung represented: "Obviously down the road, we'll eventually need probably more distribution capabilities to continue support[ing] the growth, but that's more of a future down the road within the 5-year plan, but not directly related within the next, call it, 12 months or so."

95. With hundreds of containers of product that had been intended for Halloween and Christmas holiday sales and timed content releases sitting unopened in its Buckeye DC parking lot, Funko needed a solution. Despite Fall Jung's statement to investors less than two weeks earlier that Funko would not need additional distribution capabilities for at least a year, by the end of September, Funko had hired third-party logistics company Unis in nearby Goodyear, Arizona, to store slow-moving and dead inventory. Within a few months, they had filled their space in the first Unis warehouse and had rented space in a second for the remaining slow-moving and dead

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inventory. Altogether, that inventory took up between ***300,000 and 400,000 square feet*** of space – an amount of product equivalent to 1/3 to 1/2 the square footage of the Buckeye DC.

5. Defendants' Execution Problems Are Brought to Light and Funko's Share Price Plummets

96. Following Funko's enthusiastic Investor Day in September, and with the high SG&A spend of 1H22 supposedly over, analysts were optimistic for the Company's 3Q22 results and updated FY22 guidance.

97. Those expectations were soon smashed, however, when Funko filed a Form 8-K and Form 8-K/A with the SEC, both signed by Fall Jung, announcing its 3Q22 results on November 3, 2022. While sales in 3Q22 exceeded analyst expectations, net income margin decreased 390 basis points to just 3%, adjusted EBITDA margin decreased 520 basis points to 9.8%, and SG&A costs were a whopping $97.9 million, supposedly due to "increased infrastructure investment to accommodate recent rapid growth and provide capacity for sustained future growth." Adjusted earnings per diluted share for the quarter missed analyst consensus by nearly 45%, while inventories were $265.8 million – an increase of $31.8 million, or 13.5%, over 2Q22 levels, and ***88.7% higher*** than at the end of 3Q21. The Company also reduced its 2022 financial guidance, telling investors to expect "[s]equential decline in gross margin due to margin seasonality and ongoing inventory management"; adjusted EBITDA margin of high single digits instead of the previously guided 14.6%; adjusted net income of $39 million to $41 million (previously $101.8 million to $107.3 million); and adjusted earnings per diluted share of $0.70 to $0.80 (previously $1.88 to $1.99).

98. The Company's Form 10-Q for 3Q22, signed by Fall Jung and certified by both Perlmutter and Fall Jung, also disclosed that Funko management had identified material weaknesses in the Company's financial control over financial reporting, such that there was a reasonable possibility that a material misstatement of the Company's annual or interim financial

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statements would not be prevented or detected on a timely basis. Specifically, the deficiencies related to Funko's general information technology controls ("GITCs"), due to,

> ineffectively designed and implemented user access controls and segregation of duties controls within information technology systems utilized by the Company in its financial reporting. As such, certain manual and automated business process controls were deemed ineffective because they are dependent on the affected GITCs or rely on information from the impacted systems.

The Form 10-Q also noted that there had been "no changes in our internal control over financial reporting during the quarter ended September 30, 2022" – meaning that the same deficient internal controls had been present in 2Q22 as well.

99. On the Company's 3Q22 earnings call later that day, Perlmutter finally admitted that Funko's DC had been designed to run on the Oracle WMS, that Funko had elected to open the DC before Oracle was ready, and that the Company's "higher-than-expected short-term operating expenses" had caused the lowered EBITDA margin guidance. Fall Jung acknowledged that the "higher expenses consisted primarily of greater labor costs within the facility and additional machinery to support product movement" and that in 3Q22, the additional investment in labor alone reduced adjusted EBITDA by approximately $5 million, while SG&A had increased to 27% of sales. And, despite having stated just weeks earlier that Funko would not need additional operational capacity for at least 12 months, Fall Jung now informed investors that the Company had also added third-party logistics warehouse space in 3Q22. She also stated that Defendants expected the SG&A investment impact on Funko's margin profile to largely persist until the completion of the belated ERP implementation, and that the Company had taken on additional debt in order "to support the near-term infrastructure investments and offset our increased working capital needs stemming from our inventory timing." More, the Company expected SG&A costs in 4Q22 to be even ***higher*** than in 3Q22.

100. With respect to the Company's bloated inventory levels, Fall Jung still misleadingly asserted that the inventory was "generally high quality," and that Funko would "continue to work

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through inventory levels and expect to make sequential progress." In response to analyst questions about the inventory, Fall Jung continued to downplay the severity of Funko's problems, claiming that "yes, it is up year-over-year," but "last year was a pretty tight inventory environment because we were dealing with the supply chain challenges."

101. Asked by an incredulous analyst, "this infrastructure thing, how did it become a surprise," Perlmutter lamely responded:

> It was a – we launched the new warehouse. We made the decision to move the new warehouse with a delayed ERP and part of that ERP is what's called WMS, which is warehouse management software thing. And basically, that's how you optimize the layout of that warehouse. And so when that ERP is [delayed], it came with the extra work around having to create manual processes to optimize that warehouse, which would normally have been done in an operating system, but unfortunately, we didn't have.
>
> So that's – was it a surprise? I would say it caused us more manual processes than we expected. So yes, I think that, that was something that caught us a little bit off guard. But obviously, we're pushing through and we're creating the manual workarounds to continue to get that revenue [out] the door.

Fall Jung added: "[G]iven that we did launch it in Q2, we did expect, any new DC, we did expect hiccups around the launch of it, what I think is the bigger – unfortunate part is that they continued on whereas we expected them in the Q2."

102. Analysts were floored by the revelations, and clearly were not assuaged by Defendants' claims that these expenses were truly "surprise[s]." In its November 3, 2022 report, Truist Securities ("Truist") stated: "Not only do we have little confidence in the company's ability to deliver on near-term goals but elevated inventory and higher costs currently impairs any type of visibility well into 2023. We also believe ***a credibility issue could weigh on shares over the foreseeable future*** . . . ." The Truist report further stated: "***[T]onight's commentary/guidance was inexplicable, to us***. . . . Not only had FNKO provided guidance nearly 1/2 way through 3Q, but management hosted an investor event just 7 weeks ago where it outlined lofty L-T financial targets." In its November 4, 2022 report, D.A. Davidson stated, "***[i]t feels like we were hit with a***

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bomb" and "[w]e think ***FNKO should have made disclosures at its investor day***." BMO Capital Markets' ("BMO") November 4, 2022 report noted that: "FNKO reduced 2022 sales guidance, as all toy companies have done, but slashed profit outlook due to higher than expected infrastructure investment expense. After hosting an investor day in September, this revised outlook caught investors off guard."

103. Following Funko's November 3, 2022 disclosures, Funko's stock dropped an astounding ***59%***, closing at $7.92 per share on November 4, 2022, from a prior day close of $19.50.

104. The Funko Board, led by the TCG Investor Consortium, swiftly made changes in the C-Suite. On December 5, 2022, Funko issued a press release announcing "a series of leadership changes to strengthen the Company's operations, drive enhanced returns for stockholders and best position Funko to capture the significant opportunities ahead." Perlmutter was demoted back to President effective immediately, where he would once again "focus primarily on growing the Company's brands." Fall Jung "stepp[ed] down" as CFO, effective immediately. Since the transition had not been planned and the Board had no replacement candidate in mind, the Board retained an interim CFO, Scott Yessner, through a talent services firm. The Board brought back Mariotti, former CEO and current Chief Creative Officer, as CEO. Mariotti had "a mandate from the Board to identify operational improvements while continuing to drive profitable growth." Finally, the Board created a new "Chief Operating Officer" role and retained Steve Nave as a consultant to focus on operations. On March 1, 2023, the Company issued a press release announcing that Steve Nave had been hired to be both the Company's CFO and its COO.

105. In a separate release issued March 1, 2023 on Form 8-K, Funko reported its 4Q22 and FY22 financial results. The release claimed that during the quarter, Funko had "made progress in addressing operational issues that impacted our results in the second half of 2022," and "strengthened our executive and operational management team and have taken significant steps to improve our operating efficiency." Nevertheless, in 4Q22, net income decreased ***368%*** year-over-year, adjusted EBITDA decreased 116% year-over-year, gross margin was just 28.3% versus

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analyst consensus of 32.7%, and the Company experienced an adjusted loss per diluted share of $(0.35).

106. Net income for FY22 decreased ***108%*** compared to FY21, adjusted EBITDA margin decreased 720 bps, to 7.4% (approximately ***half*** of what Funko had guided to 3/4 of the way through FY22). Meanwhile, the Company's adjusted earnings per diluted share for FY22 was just $0.57 – approximately ***20% lower*** than the ***reduced*** $0.70 to $0.80 the Company had guided to in November. The Company also announced that, far from implementing the Oracle project in early 2023, as represented in November, the Company had decided to abandon the Oracle ERP project completely, taking a ***$32.5 million write down*** of capitalized costs associated with the years-long project. The Company also announced that it intended to eliminate and write down ***$30 million to $36 million*** of Funko inventory in the first half of 2023 in order to "manag[e] inventory levels to align with the operating capacity of our distribution center."

107. Speaking on the Company's earnings call that day, Mariotti told analysts that, "[i]t was clear on our last earnings call that the business and our operations hit an inflection point, a combination of macro factors and Funko-specific issues have disrupted our financial and operating performance to an unacceptable degree." He acknowledged that:

> ***We are beyond the intended capacity of our Arizona-based distribution center***. The volume is restricting our distribution center's throughput and incurring incremental container rental charges. By eliminating this inventory, which we expect to do in the first half of this year, we expect that we'll both reduce SG&A expenses and improve our gross margin by saving on incremental container rental charges.

Describing 4Q22's 28% gross margin, Nave attributed the shortfall to "container rental charges and, to a lesser extent, charge-backs," that the "container rental charges [were] incurred when capacity constraints within our distribution center prevented us from unloading containers," and disclosing that "***[t]hese 2 factors reduced gross profit by approximately $15 million***."

108. Nave also spoke on the Company's abandonment of the Oracle project, stating, "[w]e figured out in early part of this year, let's call it, January, that we were not going to be on

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time with the launch of the ERP that was scheduled to happen this summer," and that the Company would remedy "the biggest hamstring in [its] U.S. distribution," by implementing a separate warehouse management system over the summer. Nave had been able to tell within one month of his employment as Funko's Interim COO, and five-to-six months ahead of the intended ERP implementation, that the ERP would not be ready. Meanwhile, Mariotti referred to the Oracle project as "a fairly botched ERP process."

109. Speaking about the Company's DC problems, Nave conceded that "[t]he problem with the inventory is it just became too cumbersome to operate in any sort of efficient manner. . . . It's been incredibly inefficient both because of the system issue as well as the inventory starting to pile up." Asked by an analyst from BMO whether "now that you've stepped into this role and you had a look under the hood, do you have confidence in Funko's systems and ability to track that inventory?" Nave effectively said ***no***:

> My confidence level, yes, ***we don't have the best systems right now***, which is why we talked about things like an ERP and a warehouse management system. So I have confidence that ***we're going to get to a place where our systems infrastructure supports the business the way it needs to***.

110. Following these revelations, Funko's Class A stock price closed at $9.94 on March 2, 2023 from a prior day close of $10.70 as the remaining inflation from Defendants' left Funko's share price.

H. Post-Class Period Events Further Illustrate the Depth of Funko's Class Period Problems

111. Shortly after the earnings call, pictures emerged online of hundreds of boxes of Funko product sitting in a landfill, which quickly went viral as media outlets and individuals reported or commented on the negative environmental impact of the move, among other aspects of Funko's decision. Unsurprisingly, Buckeye employees were still unpacking now-unsellable Christmas-themed inventory that had been sitting in the parking lot containers for months.

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112. Then, on July 13, 2023, Funko issued a press release on Form 8-K announcing that Mariotti had "agreed to take a six month leave of absence from the Company and cease serving as Chief Executive Officer, effective immediately," though he would remain a member of the Board of Directors. It stated that "[o]n the Effective Date, the Company's Board . . . removed Mr. Mariotti from the office of Chief Executive Officer and appointed [Board member] Michael Lunsford as the Company's Interim Chief Executive Officer."

113. On the Company's August 3, 2023 2Q23 earnings call, Lunsford stated that his "mandate from the Board [is] to quickly reshape Funko to regain its nimbleness to return to growth and to be meaningfully more profitable." The Company also announced that it was conducting its second round of layoffs in the year (the first having occurred in February 2023), so that as of August, the Company had laid off 23% of its workforce for annualized savings of $30 million. Nave also stated that:

> [W]e're planning the back half of the year from an inventory perspective, a little bit different than what we've done in the past. What we've done in the past is we've always wanted to make sure that we were in stock for our retail partners. And this time around, we're willing to leave a little bit of sales on the table if things really rebound so that we don't end up in another inventory position like we were at the end of last year.

V. DEFENDANTS' MATERIALLY FALSE AND MISLEADING STATEMENTS AND OMISSIONS

A. March 3, 2022

114. On March 3, 2022, Funko filed a Form 10-K announcing financial results for the year ending December 31, 2021, and signed and certified by Perlmutter and Fall Jung. Included among the "Risk Factors" disclosed in the filing was the following:

> **Our success depends, in part, on our ability to successfully manage our inventories**. We must maintain sufficient inventory levels to operate our business successfully, but we must also avoid accumulating excess inventory, which increases working capital needs and lowers gross margin.

* * *

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> ***If demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard***. For example, in the fourth quarter of 2019, we wrote-down $16.8 million of inventory due to our decision to dispose of slower moving inventory to increase operational capacity which contributed to the Company's net loss for the period."

115. In its Form 8-K filed the same day, which was signed by Fall Jung, the Company provided detail on the year's SG&A outlook. Fall Jung was quoted as saying, "SG&A as a percent of sales is also expected to be ***slightly higher in the first half of the year*** due to the timing of project costs associated with consolidation and relocation of our U.S.-based distribution centers and our ERP implementation."

116. Also on March 3, 2022, Funko held its 4Q21 earnings call. During the call – Perlmutter's first as CEO of Funko – Perlmutter provided financial guidance for 2022 that exceeded analyst consensus expectations, stating:

> For 2022, we anticipate revenue growth of between 20% and 25% and adjusted EPS of $1.75 to $1.91, with adjusted EBITDA margin relatively in line with fiscal 2021, reflecting onetime project spend that Jen will describe in detail as well as freight headwinds that we are now expecting to remain in place for most of the year. Despite external factors that are largely out of our control, ***we've proven our ability to deliver in difficult environments, and I'm very confident we are well positioned to meet our objectives for the full year***.

117. Also during the call, Fall Jung told analysts and investors: "We expect our adjusted EBITDA margin to be relatively in line with 2021 [14.6%], reflecting a significant freight inflation headwinds as well as ***approximately 80 basis points of pressure due to onetime product spend from the consolidation and relocation of our distribution centers and our new ERP system***."

118. An analyst from Jefferies asked Fall Jung: "You gave 80 basis points of pressure from – it seems like more of a transitory DC and ERP implementation and transition. Any context on when that 80 basis points is concentrated? Is it first half, second half? Anything we should be mindful of?" Fall Jung replied: "***Yes. Yes, first half, for sure. [W]e will probably launch in the***

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beginning[,] early . . . Q3 for the ERP, but the distribution center move will happen in the first half."

119. The statements detailed above in ¶¶114-118 were materially false and misleading when made. As Defendants knew or recklessly disregarded:

(a) Contrary to Fall Jung's statements in ¶¶115, 117-118, there was no way that the costs from "consolidation and relocation of our distribution centers and our new ERP system" would be "slightly higher" or limited to "approximately 80 basis points of pressure" that would "for sure" be concentrated in the first half of 2022. Actually, as Defendants were aware at the time they made these statements, the Buckeye DC was designed to run on Oracle WMS, without which the massive warehouse could not be run efficiently. This software was part of the Oracle integration, which Defendants knew would not be ready for implementation by summer 2022. More, Funko's lease on the Buckeye warehouse would only start at the beginning of April 2022, and they had not yet built out the necessary rack space, obtained permitting for the needed rack space, hired or trained the requisite additional warehouse workers, or obtained the equipment necessary for the DC to function at even moderate efficiency. This, combined with the sheer amount of inventory that was being transferred from the five Washington warehouses and the amount of inventory that was currently stuck in transit but ***would*** be sent to Buckeye when it was released made it a near certainty that costs related to getting the DC operational and productive would extend well beyond 2Q22. *See* §§IV.C-IV.G.1.

(b) Contrary to the statements in ¶¶115-116, 118, it was well-understood inside Funko that the Oracle project was not going to be ready by the end of 2Q22 or beginning of 3Q22. Not only was the C-Suite not aligned on how the ERP system should function, making it impossible for the integration team to complete the system architecture, but more than a year into the Oracle project, Funko's data was still far from being "clean" enough to transfer to a new ERP system, something an employee had voiced to Fall Jung weeks earlier. Meanwhile, the Company's Microsoft NAV system was antiquated and unable to handle the workload of Funko's growing

operations reliably. The Company was therefore not "well positioned to meet our objectives for the full year." *See* §§IV.C-IV.G.1.

(c) Although in ¶114 Defendants warned of a ***possible*** risk of having excess inventory "that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard," that "risk" had ***already materialized*** – each of Funko's five Washington warehouses carried a significant amount of dead and aged inventory accumulated over at least two years that Defendants knew they were not able to sell. In EV1, the Company's largest Washington distribution facility, approximately 25% of the inventory housed was dead. *See* §IV.G.2.

B. May 5, 2022

120. On May 5, 2022, Funko filed a press release on Form 8-K with the SEC, signed by Fall Jung, announcing its financial results for 1Q22 and reiterating its previously announced FY22 guidance. Specifically: "Adjusted EBITDA margin of approximately 14.6% at the midpoint of our revenue range. This reflects ongoing transocean freight inflation, as well as ***approximately 80 bps of headwind from one-time project spend associated with the consolidation and relocation of our U.S.-based distribution center and the implementation of our new ERP system***."

121. The press release also stated that:

> In the second quarter of 2022, the Company anticipates the following results: . . . SG&A as percent of net sales to increase sequentially, reflecting ***one-time project spend on our distribution center relocation, and ERP implementation***; and [l]ower gross margin and higher SG&A as a percent of sales, which are expected to reduce adjusted EBITDA margin sequentially ***before recovering in the second half of this year***.

122. In its Form 10-Q for 1Q22 filed the same day, signed and certified by Perlmutter and Fall Jung, Funko included the following "Risk Factor":

> ***Failure to successfully operate our information systems and implement new technology effectively could disrupt our business or reduce our sales or profitability***.
>
> We rely extensively on various information technology systems and software applications, including our enterprise resource planning software, to manage many aspects of our business, including product development,

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> management of our supply chain, sale and delivery of our products, financial reporting and various other processes and transactions. We are critically dependent on the integrity, security and consistent operations of these systems and related back-up systems. . . . ***The failure of these information systems to perform as designed, our failure to operate them effectively, or a security breach or disruption in operation of our information systems could disrupt our business***, require significant capital investments to remediate a problem or subject us to liability. We are also in process of upgrading our enterprise resource planning software globally, beginning in the United States. ***If the potential upgrades are not successful or result in delays, our business could be disrupted or harmed.***

123. Another "Risk Factor" stated:

> **Our success depends, in part, on our ability to successfully manage our inventories**.
>
> We must maintain sufficient inventory levels to operate our business successfully, but we must also avoid accumulating excess inventory, which increases working capital needs and lowers gross margin. . . .
>
> ***If demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard***. For example, in the fourth quarter of 2019, we wrote-down $16.8 million of inventory due to our decision to dispose of slower moving inventory to increase operational capacity which contributed to the Company's net loss for the period.

124. Also on May 5, 2022, Funko held its 1Q22 earnings call. During the call, Fall Jung again asserted that:

> ***[W]e remain on track to deliver full year adjusted EBITDA margins consistent with 2021***. This target reflects the ongoing freight inflation headwinds as well as ***approximately 80 basis points of pressure due to onetime project spend from the consolidation and relocation of our distribution centers and the implementation of our ERP system***.

125. Later on the call, Fall Jung had the following exchange with a market analyst from Jefferies:

> **[Q.:]** And then, Jen, one for you is just on your remarks around the onetime project spend for ERP and DC (inaudible) can you just help us think through the total amount that you anticipate spending? And then anything more by cadence by quarter would be really helpful.
>
> **[Fall Jung:]** Yes. Thanks for the question. So yes, we reported out that ***was about 80 basis points on the year, all of which will happen in the first half of the***

> ***year. It's about 2 points of pressure just in Q2 on adjusted EBITDA. So we're launching – or we did launch the new DC in April, and the ERP is set to come out at the end of the quarter***.
>
> **[Q.:]** Okay. So anything trickling into the back half? Or should we assume that it's pretty much done after Q2?
>
> **[Fall Jung:]** Yes. ***It's really the pressure[']s all in the first half of the year, specifically Q2***.

126. Answering additional analyst questions regarding Funko's gross margin, Fall Jung again reiterated that the SG&A cost pressure would be focused in 2Q22: "So unfortunately, it's a bit of a hockey stick on the margin front, the way it looks. ***But Q2 is where we're seeing the pressure from the net SG&A perspective on the investments*** as well as on pressure from freight."

127. The statements detailed above in ¶¶120-126 were materially false and misleading when made. As Defendants knew or recklessly disregarded:

(a) Although in ¶123 Defendants warned of a ***possible*** risk of having excess inventory "that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard," that "risk" had ***already materialized*** – each of Funko's five Washington warehouses carried a significant amount of dead and aged inventory accumulated over at least two years that Defendants knew they were not able to sell – an estimated 25-30% of inventory in the Washington warehouses as of April 2022. Beginning in April, this dead inventory had been transferred to the Buckeye DC, where it was taking up rack and floor space that was at a premium and needed for new (and sellable) products. *See* §IV.G.2.

(b) Defendants' statement in ¶122 that "business ***could*** be disrupted or harmed" if the ERP system upgrades were "not successful or result in delays," was materially misleading, as that risk had already materialized as well. The Oracle ERP was originally intended to launch at the same time as the Buckeye DC, and the Buckeye DC was designed around the Oracle ERP system. When it was apparent by early 2022 that the ERP would not be ready for implementation by the April opening of the DC, the Company decided to plow forward and open the DC anyway,

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with disastrous effect. At the time this "risk factor" was issued, the DC was already experiencing problems with inventory not being checked in or out properly and so being lost within the facility and the inventory layout floor plan designed by the Oracle team was inefficient and unusable. *See* §§IV.F-IV.G.2.

(c) Funko's assertion in ¶122 that "failure to successfully operate our information systems and implement new technology effectively ***could*** disrupt our business" was also a risk that had already materialized. Its antiquated systems were inadequate to run the Company's operations, including inventory tracking, as CFO/COO Nave later admitted. The data contained within the existing system was incomplete and often inaccurate, requiring Sales and S&OP employees to engage in manual workarounds and disrupting the Oracle integration process. And, by the time that Defendants published this statement, the Buckeye DC had abandoned using NAV to verify inventory accounts or check inventory into the warehouse due to its inconsistent data, failure to update, and inability to handle the workload that the Buckeye DC needed it to perform. As a result, product was being "lost" in transfer and in the DC, causing problems fulfilling orders. *See* §§IV.C-F, IV.G.1-2.

(d) Contrary to Fall Jung's representation in ¶125, it was well-understood inside Funko that the Oracle project was not going to be ready by the "end of the quarter [2Q22]." Not only was the C-Suite not aligned on how the ERP system should function, making it impossible for the integration team to complete the system architecture, but more than a year into the Oracle project, Funko's data was still far from being "clean" enough to transfer to a new ERP system, something an employee had voiced to Fall Jung weeks earlier. *See* §§IV.C-F.

(e) Contrary to the statements in ¶¶120-121, 124-126, there was no way that the costs from "consolidation and relocation of our distribution centers and our new ERP system" would be limited to "approximately 80 basis points of pressure[,]" "all of which will happen in the first half of the year." Actually, as Defendants were aware at the time they made these statements, the Buckeye DC was designed to run on Warehouse Management Software, without which the

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massive warehouse could not be run efficiently. Because this software was part of the Oracle integration, which Defendants knew would not be ready for implementation by summer 2022, Defendants could not reasonably say that costs from the relocation would be limited to the first half of the year. Meanwhile, as discussed in ¶127(d), above, the Oracle integration was far from being completed. In fact, the entire project would end up being abandoned at a cost of $32.5 million in 4Q22, in part because it was not going to be ready for implementation in summer ***2023***. More, Funko's lease on the Buckeye warehouse only started at the beginning of April 2022, and they had not yet built out the necessary rack space, obtained permitting for the needed rack space, hired or trained the requisite additional warehouse workers, or obtained the equipment necessary for the DC to function at even moderate efficiency. This, combined with the sheer amount of inventory that was being transferred from the five Washington warehouses and the amount of inventory that was currently stuck in transit but ***would*** be sent to Buckeye when it was released made it a near certainty that costs related to getting the DC operational and productive would extend well beyond 2Q22. *See* §§IV.C-F, IV.G.1-2, IV.G.5.

C. August 4, 2022

128. On August 4, 2022, Funko filed its Form 10-Q for 2Q22, signed and certified by Perlmutter and Fall Jung. The 10-Q once again included "risk factors" regarding its inventories. Specifically:

> **Our success depends, in part, on our ability to successfully manage our inventories**.
>
> We must maintain sufficient inventory levels to operate our business successfully, but we must also avoid accumulating excess inventory, which increases working capital needs and lowers gross margin. . . . We have recently experienced canceled orders and if demand or future sales do not reach forecasted levels, ***we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard***. For example, in the fourth quarter of 2019, we wrote-down $16.8 million of inventory due to our decision to dispose of slower moving inventory to increase operational capacity which contributed to the Company's net loss for the period. ***If we are not successful in managing our inventory, our business, financial condition and results of operations could be adversely affected***."

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129. Funko's 10-Q also repeated that: "Failure to successfully operate [its] information systems and implement new technology effectively could disrupt our business or reduce [its] sales or profitability," was a "risk factor." Specifically, the Form 10-Q stated:

> We rely extensively on various information technology systems and software applications, including our enterprise resource planning software, to manage many aspects of our business, including product development, management of our supply chain, sale and delivery of our products, financial reporting and various other processes and transactions. . . . The efficient operation and successful growth of our business depends on these information systems, including our ability to operate and upgrade them effectively and to select and implement adequate disaster recovery systems successfully. ***The failure of these information systems to perform as designed, our failure to operate them effectively, or a security breach or disruption in operation of our information systems could disrupt our business***, require significant capital investments to remediate a problem or subject us to liability. We are also in process of upgrading our enterprise resource planning software globally, beginning in the United States. In August 2022, we announced that we are delaying the remaining steps for implementation of our enterprise resource planning software to 2023. ***If the potential upgrades are not successful or result in further delays, our business could be disrupted or harmed***."

130. The Company's 2Q22 Form 10-Q, also disclosed for the first time that the Company "expect[ed] personnel and related costs to remain elevated through at least the end of 2022 to support the ***final transitions*** of our U.S. distribution warehouses, ***additional personnel to support strategic initiatives and overall business growth*** and due to additional inflationary pressures to increase wages, commissions and benefits expenses," and "also expect[ed] elevated costs related to our enterprise resource planning ('ERP') implementation ***as we expect to finalize the remaining steps in early 2023***."

131. Perlmutter and Fall Jung also signed and submitted SOX certifications with the 2Q22 Form 10-Q which stated in relevant part that:

> Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

* * *

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> ***The registrant's other certifying officer and I have disclosed***, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
>
> (a) ***All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information***; and
>
> (b) ***Any fraud, whether or not material***, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

132. In its August 4, 2022 Form 8-K, signed by Fall Jung, Funko reported that: "Inventories at the end of the second quarter of 2022 totaled $234.0 million, ***up 170.9% compared to a year ago, reflecting receipt of delayed inventory*** as pandemic-related supply chain disruptions began to improve toward the end of the quarter."

133. After market close on August 4, 2022, Funko held its 2Q22 earnings call. On the call, Fall Jung misleadingly stated that:

> SG&A for the quarter was $83 million or 26% of net sales. In Q2, we saw elevated expenses related to the relocation of our distribution center from Everett to Buckeye, Arizona as well as our ERP project. Regarding our ERP, we recently made the difficult decision to delay the remaining steps until 2023. There were a number of factors that contributed to this decision, but ***ultimately, we did not want to impair the momentum that we have today*** by shifting to a platform that we felt wasn't yet fully ready to support our business. We plan to have more details for you around our 2023 implementation plans on our Q3 call in November.

134. Later, speaking to the Company's bloated inventory levels, Fall Jung stated:

> Inventory at quarter end totaled $234 million as shipping delays began to subside. While our inventory levels are up year-over-year, ***we believe that inventory is generally high quality and leave us well positioned to meet our consumer demand and support our strong second half growth forecast***.

135. In an exchange with a Jefferies analyst, Fall Jung reiterated that the inventory was in a "healthy position":

> **[Q.:]** Jen, the first is on inventory. Just to give you a chance to talk a little bit more about where the inventory resides, how much of it is related to the DC relocation?

> How much might be in transit? If you could just dimensionalize inventory for us, that would be appreciated.
>
> **[Fall Jung:]** Great. Yes, inventory, so what we actually ended up, as you know, in Q4, had a lot of delays that rolled into Q1 just due to the congestion within the supply chain. And you're seeing a little bit of that in Q2 as well. ***Although as we're now looking into the back half of the year, we feel the inventory is in a really good healthy position, and we're poised to deliver on our back half results. It was really about just managing through the congestion that we saw so far***. Knowing that, we're seeing those transit times come down and delivery dates to be more on time than they had earlier in the year. ***So there is a large portion of the in-transit, but we're working to get that into the DC and get that out to our customers***.

136. In a separate exchange with an analyst from D.A. Davidson, Fall Jung was asked about the delayed Oracle implementation and what it meant for SG&A costs:

> **[Q.:]** And also on the cost side, you've talked about pushing out this ERP initiative into 2023. Does that mean there's going to be less associated SG&A costs associated with that in 2022?
>
> **[Fall Jung:]** No, and that's actually a great question. There'll be puts and takes about 2022. We will still continue to work on these initiatives throughout the year. So the run rate will continue. But there's other offsetting factors to that. ***So we don't see it as a major headwind in 2022 so far, but we feel good we made the right decision for the business to not have business interruption as we go into the holiday season***.

137. Asked whether "in 2022, do you have any sense for whether like your cash flow can be up or down year-over-year[,]" Fall Jung misleadingly replied:

> What you're seeing underneath the covers there [are] a couple high [uses] of cash, whether it be ***the distribution center, that was a major feat to get that up and running*** . . . then we had the inventory that came in all at once as you got in Q4 inventory, Q1 inventory. ***And so (inaudible) inventory and some of the uses of cash is what you're seeing***.

138. The statements detailed above in ¶¶128-137 were materially false and misleading when made. As Defendants knew or recklessly disregarded:

(a) Contrary to Defendants' statement in ¶128 warning of a ***possible*** risk of having excess inventory "that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard," that "risk" had ***already materialized*** – each of Funko's five

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Washington warehouses carried a significant amount of dead and aged inventory accumulated over at least two years that Defendants knew they were not able to sell – an estimated 25-30% of inventory in the Washington warehouses as of April 2022. This dead inventory had been transferred to the Buckeye DC, where it was taking up rack and floor space that was at a premium and needed for new (and sellable) products. More, as hundreds of shipping containers of inventory delayed since as long ago as 4Q22 (approximately 10 months earlier) sat in Funko's parking lot unable to be unloaded due to the inventory congestion at the DC, the amount of aging, unsellable and dead inventory Funko further accumulated. Fall Jung's statements in ¶¶132 and 134-135 attributing the increase in Funko's inventory solely to "receipt of delayed inventory" or suggesting inventory was "in a healthy position" and "generally high quality" omitted or misrepresented these material facts. *See* §§IV.G.1-4.

(b) Defendants' statement in ¶129 that "business ***could*** be disrupted or harmed" if the ERP system upgrades were "not successful or result in delays," was materially misleading, as that risk had already materialized as well. The Oracle ERP was originally intended to launch at the same time as the Buckeye DC, and the Buckeye DC was designed around the Oracle ERP system. When it was apparent by early 2022 that the ERP would not be ready for implementation by the April opening of the DC, the Company decided to plow forward and open the DC anyway, with disastrous effect. At the time this "risk factor" was issued, the lack of WMS at the Buckeye DC was wreaking havoc, with inventory not being checked in or out properly and so being lost within the facility, and Pickers unable to find product needed for orders within the facility, such that partially collected orders littered the warehouse floor. By August 2022, the DC was more than 50 days behind in shipping customer orders. *See* §§IV.C-F, IV.G.1-G.4.

(c) Funko's assertion in ¶129 that "failure to successfully operate our information systems and implement new technology effectively ***could*** disrupt our business" was also a risk that had already materialized. Its antiquated ERP was inadequate to run the Company's operations, as CFO/COO Nave later admitted. The data contained within the existing system was

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incomplete and often inaccurate, requiring Sales and S&OP employees to engage in manual workarounds and disrupting the Oracle integration process. And, by the time that Defendants published this statement, the Buckeye DC had abandoned using NAV to verify inventory accounts or check inventory into the warehouse due to its inconsistent data, failure to update, and inability to handle the workload that the Buckeye DC needed it to perform. As a result, product was being "lost" in transfer and in the DC, causing problems fulfilling orders. *See* §§IV.C-G.

(d) Contrary to Funko's statement in ¶130 that the Company expected elevated costs through the end of 2022 in order to "support the final transitions" of its distribution facilities and to "finaliz[e]" the Oracle ERP system, Funko actually expected those elevated costs because the Buckeye DC was in chaos, with 300 to 500 rented shipping containers accruing extremely high rental fees and late charges as they sat unloaded in Funko's Buckeye parking lot. More, because the DC did not have the WMS it was designed to run on or the equipment that workers needed to efficiently fulfill orders, Funko had needed to hired additional manpower to get the DC up to even a minimal level of productivity. *See* §§IV.G.1-G-4.

(e) Contrary to Perlmutter's and Fall Jung's SOX certifications (¶131), the Company had undisclosed material weaknesses in its internal control over financial reporting, particularly with respect to the Company's General Information Technology Controls ("GITCs"), as it would soon admit in its 3Q22 Form 10-Q. Specifically, the Company had ineffectively designed and implemented user access controls and segregation of duties controls within information technology systems utilized by the Company in its financial reporting. This was certainly the case in the Microsoft NAV system, where new hires' NAV credentials were created by simply mirroring the user permissions of other employees without the imposition of any controls to limit their specific access to modify existing entries. This was a major problem, as it allowed any warehouse employee to change inventory counts and other critical information that the Company's financials depended upon, potentially undermining the reliability or accuracy of their SEC reporting. *See* §IV.G.2.

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(f) Fall Jung's assertions in ¶133 that the ERP implementation had been pushed to 2023 because "ultimately, we did not want to impair the momentum that we have today" and in order to "not have business interruption as we go into the holiday season" blatantly ignored the ongoing chaos at the Buckeye DC. Far from experiencing "momentum," the Company's distribution capabilities had been crippled by the lack of WMS in the Buckeye DC, and the facility was completely overrun with inventory that had been stored haphazardly and was unable to be located, as well as pallets of partial orders that could not be completed until missing inventory was located. There were hundreds of unloaded shipping containers that contained inventory that could not be placed in the DC, and so did not register as "in-stock" for order fulfillment. The Company was more than 50 days behind in fulfilling orders by the end of 2Q22, and at least some retail orders had been decreased or cancelled altogether due to the delays. More, the ERP implementation was not pushed in order to avoid interrupting the holidays; the system had never been ready to implement in 2Q22, and in fact, would ultimately end up being abandoned at a cost of $33 million in 4Q22, in part because it was not going to be ready for implementation in summer ***2023***. *See* §IV.G.

(g) Contrary to Fall Jung's claim in ¶136 that SG&A spend due to the delayed ERP implementation would not pose "a major headwind in 2022" omitted the ongoing costs of operating the Buckeye DC without the WMS software it was designed around, and which had already cost the Company millions in additional labor and cancelled orders. *See* §IV.G.2-4;

(h) Fall Jung's statement in ¶137 that the Company had spent significant cash on the Buckeye DC, which "was a major feat to get that up and running" misleadingly implied that the cash spent had been sufficient to get the Buckeye DC up and running. In reality it was barely functional, well over capacity with hundreds of shipping containers unable to be unloaded, and would require significantly more SG&A spend in future quarters to obtain the necessary equipment, labor, and space for the warehouse to actually be efficiently functional. *See* §IV.G.4.

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(i) Fall Jung's statement in ¶135 that a large portion of the Company's inventory was "in-transit, but we're working to get that into the DC and get that out to our customers" concealed the true state of Funko's inventory management: the problem was no longer that inventory was stuck in port due to COVID 19-related delays, nor was inventory "congestion" a problem of the past. Instead, by July 2022, ***hundreds*** of the "in-transit" containers of inventory had actually arrived at Funko's Buckeye DC, but were simply sitting in the parking lot, continuing to accrue rental fees because there was nowhere for workers to unload the inventory. The inventory was only considered "in-transit" because it couldn't be physically placed in the warehouse; without being unloaded, that inventory could not be considered "in-stock" or be able to be shipped to customers. *See* §IV.G.4.

D. September 13, 2022

139. On September 13, 2022, Funko held its first ever Press and Investor Day. Speaking to what would allow Funko to achieve the strategic plan presented, Perlmutter misleadingly stated:

> And then last, but certainly not least, is the ***unlock of technology to help us get where we're going faster and better. And that's some of the investments that we've made this year***, and that we're always keeping a look at, keeping our eye on. What are the next investments we need to do to ensure our success and ensure this growth.

140. Later in the call, a participant asked: "SG&A as a percentage of revenue has increased a bit over the past few years. How does that trend reverse? And what's the biggest source of operating leverage for you?" Fall Jung responded:

> Yes. ***What you saw for the first half of the year so far in this year is really the investments that we've made in the ERP as well as in the distribution center***. So we've been making investments for the future, and those have been coming in on the P&L. But as we look forward, we did talk about operating leverage to get to our adjusted EBITDA margin of 20%. We feel we have a good path to get there.

141. Another participant asked: "Can you help us quantify how much investment is needed for that internal growth, or how much internal investment is needed for the growth?" Fall Jung answered:

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> For the most part, from a capital perspective, we have been pretty – I think you're talking about the core business growth. We've been pretty diligent about our capital. It has really been to support our tools and molds and to continue to expand our product categories. ***Obviously, down the road, we'll eventually need probably more distribution capabilities to continue support the growth, but that's more of a future down the road within the 5-year plan, but not directly related within the next, call it, 12 months or so***.

142. The statements detailed above in ¶¶139-141 were materially false and misleading when made. As Defendants knew or recklessly disregarded:

(a) Contrary to Perlmutter's statements in ¶139, Funko's investments in technology during 2022 had not "help[ed it] get where we're going faster and better." If anything, the decision to delay the Oracle implementation had decreased Funko's operational capabilities and crippled the Buckeye DC's ability to fulfill and distribute orders in a timely or efficient manner. *See* §IV.G.

(b) Fall Jung's statement in ¶140, that "[w]hat you saw for the first half of the year so far in this year is really the investments that we've made in the ERP as well as in the distribution center[,]" falsely implied that the SG&A spend in the ERP and distribution center would not continue weighing on adjusted EBITDA margin in the future. Actually, Defendants knew that it would take far more SG&A spend then had already been undertaken to resolve the problems with the Oracle ERP project and the foundering Buckeye DC, which was more than 50 days behind in shipping customer orders. *See* §§IV.G.4-5.

(c) Far from being set for distribution capabilities for the next 12 months as Fall Jung's statement in ¶141 asserted, the Buckeye DC was already way past its intended capacity, and hundreds of shipping containers were parked in the DC lot just waiting to be unloaded into the overfilled warehouse. In fact, within ***two weeks*** of Fall Jung making this statement, Funko would rent a third-party warehouse to store its aging and dead inventory, and a few weeks after that, would be forced to rent a second. *See* §§IV.G.4-5.

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E. November 3, 2022

143. On November 3, 2022, Funko filed its 3Q22 Form 10-Q, signed and certified by Perlmutter and Fall Jung. The 10-Q contained the following materially misleading "risk factor":

> **Our success depends, in part, on our ability to successfully manage our inventories**.
>
> We must maintain sufficient inventory levels to operate our business successfully, but we must also avoid accumulating excess inventory, which increases working capital needs and lowers gross margin. . . . ***We have recently experienced canceled orders and if demand or future sales do not reach forecasted levels, we could have excess inventory that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard***. For example, in the fourth quarter of 2019, we wrote-down $16.8 million of inventory due to our decision to dispose of slower moving inventory to increase operational capacity which contributed to the Company's net loss for the period. ***If we are not successful in managing our inventory, our business, financial condition and results of operations could be adversely affected***.

144. Speaking on the Company's 3Q22 earnings call later that day, Fall Jung stated that:

> Inventory at quarter end totaled $266 million. Inventory levels remain higher than the prior year, which was a particularly tight inventory environment due to port delays and supply chain congestion. ***We believe that our inventory is generally high quality***, we will continue to work through our inventory levels and expect to make sequential progress.

145. Later, an analyst from J.P. Morgan asked: "I guess, given where your inventory levels are . . . are you – do you think you're going to have to take any actions on any of your owned inventory – and how does that change how you're thinking about – or does it change how you're thinking about growing the top line double digit?" Fall Jung answered:

> As we think about our inventory, yes, it is up year-over-year. Remember, last year was a pretty tight inventory environment because we were dealing with the supply chain challenges. So there is a little bit of nuance in the number underneath the covers. That being said, we are constantly looking at the quality of our inventory, and ***we think it generally is very healthy right now***. And in the event where we have seen a pullback a little bit in Q4, ***we have been making the right edits to our inventory,*** whether it be cutting receipts or pushing receipts out to make sure that we are managing this and managing it down towards the end of the year. Definitely an area to focus thrust.

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146. The statements detailed above in ¶¶143-145 were materially false and misleading when made. As Defendants knew or recklessly disregarded:

(a) Although in ¶143, Defendants warned of a ***possible*** risk of having excess inventory "that we may need to hold for a long period of time, write down, sell at prices lower than expected or discard," that "risk" had ***already materialized*** – each of Funko's five Washington warehouses carried a significant amount of dead and aged inventory accumulated over at least two years that Defendants knew they were not able to sell – an estimated 25%-30% of inventory in the Washington warehouses as of April 2022. This dead inventory had been transferred to the Buckeye DC, where it was taking up rack and floor space that was at a premium and needed for new (and sellable) products. More, as hundreds of shipping containers of inventory delayed since as long ago as 4Q22 (approximately 10 months earlier) sat in Funko's parking lot unable to be unloaded due to the inventory congestion at the DC, the amount of aging, unsellable and dead inventory Funko further accumulated. *See* §§IV.G.2-5.

(b) Similarly, Funko's statement in ¶143 "***if*** we are not successful in managing our inventory, our business, financial condition and results of operations ***could*** be adversely affected," was also misleading, as the Company's failure to manage its inventory had resulted in hundreds of shipping containers sitting, unloaded, in the DC parking lot for months. Not only was inventory becoming dead due to expired licenses and missed windows of relevance (resulting in lack of demand), but retailers had also cancelled large orders for seasonal-themed inventory that wouldn't arrive by the intended holiday. For example, when one Account Manager asked for a large retail order of Valentine's Day inventory to be shipped by October at the latest, they were told that the earliest the warehouse could get to it was ***May 2023***, seven months later – and unsurprisingly, the customer cancelled the order. Meanwhile, Funko employees would be unloading trailers of Christmas-related inventory well into spring of 2023. Further, Funko's financial results, including its gross margin, had also been impacted by the expensive late fees and

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rental charges owed on the hundreds of shipping containers sitting in the lot, which came at a time when freight rates were exceptionally high. *See* §§IV.G.2-5.

(c) Contrary to Defendants' statements in ¶¶144-145, a significant portion of Funko's inventory was ***not*** "high quality" or "very healthy," nor had Funko been "making the right edits" to its inventory. Rather, not only was there two years' worth of dead inventory that had been shipped to Buckeye from Funko's Washington warehouses clogging up Buckeye's shelves, but the shipping containers that had arrived following delays since 4Q21 and 1Q22 contained aging product that was no longer in demand or was out of license and unable to be sold. The fact was that rather than destroy the dead and unsellable inventory, Funko had chosen to rent two additional third-party warehouses in 3Q22 and 4Q22, amounting to 300,000-400,000 square feet of storage space, to continue holding the slow-moving and dead inventory. Ultimately, within just a few months, Funko would announce the need to write-down more than ***$30 million*** of inventory – ***tens of millions of units*** of product and more than twice the amount of Funko's disastrous 2019 write-down. *See* §§IV.B, IV.G.

VI. ADDITIONAL SCIENTER ALLEGATIONS

A. The Fraud Involved Funko's Core Operations, About Which Defendants Held Themselves Out as Knowledgeable

147. Defendants' material misstatements and omissions concerned two years-long infrastructure projects that implicated the very core of Funko's operations – (i) the consolidation of ***all*** its U.S. distribution centers into a single facility, from which the vast majority of its domestic fulfillment and shipping would take place going forward, and (ii) the Company's development and implementation of its ERP across all of its global operations – as well as the Company's overall inventory levels. Because these issues were critically important to Funko and closely monitored by Defendants and market analysts, a strong inference arises that Defendants were aware of or recklessly disregarded the true facts when making false statements and/or omitting material facts regarding these areas during the Class Period.

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148. First, inventory management, including an understanding of which products were no longer selling or sellable, was a point not only of critical operational importance, but also of importance to Perlmutter's and Fall Jung's roles as CEO and CFO particularly. It was Fall Jung's Finance group that was responsible for demand planning and inventory purchasing during the Class Period. Meanwhile, as the former Sales team leader himself, Perlmutter remained actively involved with the Sales side of the Company as CEO, and had direct relationships with several of Funko's major customers. He was known internally to be attuned to what space important customers had available for Funko on their shelves and which products those customers would want (or not want). Both Perlmutter and Fall Jung attended regular meetings with senior members of the Sales, S&OP, and Fulfillment Operations teams to discuss Sales forecasts and available inventory, as well as what inventory was not selling. More, it was Fall Jung's group that had responsibility for accounting for Funko's inventory levels as a key element of the Company's balance sheet, and for reporting the change in the Company's active licenses each reporting period in the Company's SEC filings. Both Fall Jung and Perlmutter also admitted that inventory management was of critical importance to the Company: On November 3, 2022, Fall Jung told investors that "we are ***constantly*** looking at the quality of our inventory," and Perlmutter represented that "we are ***always*** looking at the health of our inventories." A strong inference can therefore be drawn that Fall Jung and Perlmutter knew, or were reckless in not knowing, of the Company's significant build-up of dead inventory throughout the Class Period.

149. Second, the Oracle ERP project implicated ***all*** of Funko's operations, and had been ongoing for two years. Beginning in 2021, there were biweekly Steering Committee meetings about the project attended by the C-Suite, and there were status reports about the project emailed to executives following the meetings. More, Perlmutter had conversations with the Oracle implementation team regarding the difficulty they were having obtaining necessary information and decisions, as well as the lack of leadership alignment on the project. The Oracle project was of such centrality that it was placed under the direct supervision of Joe Sansone, the COO. Fall

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Jung and Sansone debated various aspects of the Oracle project at the biweekly meetings, and Oracle was the system Fall Jung's Finance and Accounting teams would use to track and compile Funko's financial information once it was implemented. It was also her team that was responsible for accounting for the costs of the multiple third-party IT firms working on the project. Unquestionably, Fall Jung and Perlmutter would have been well-informed about the realistic timeline for the ERP implementation, and involved in discussions regarding whether to delay the implementation or open the Buckeye DC without Oracle.

150. Similarly, a strong inference of at least deliberate recklessness can be inferred with respect to Fall Jung's and Perlmutter's SOX certifications regarding the adequacy of the Company's GITCs: the entire Company used Microsoft NAV, the Oracle implementation team and IT employees had discussed the need to correct the user permission controls through Oracle, and the Company's inventory tracking – a key element to accurately accounting for the Company's inventory balance and revenue recognition – had completely unraveled at Buckeye beginning in spring 2022, in part due to the fact that individual employees could access and change inventory counts within NAV. Fall Jung and Perlmutter would have been aware of the material weaknesses in the Company's internal control over financial reporting by at least June 2022, had they done the controls review their SOX certifications required.

151. Third, the Buckeye DC was not only the largest distribution center that the Company had ever built, but it was the primary hub for the vast majority of Funko's domestic shipping (all product aside from Loungefly). Fall Jung's team was involved in helping to plan the storage needed for projected inventory levels prior to the warehouse opening, as well as accounting for the costs of consolidating five warehouses into one single facility. More fundamentally, it was a simple fact of Funko's business that if orders could not or were not shipping, then the Company could not recognize revenue on those orders – and Funko's revenues were of the utmost importance to both Perlmutter as CEO and Fall Jung as CFO.

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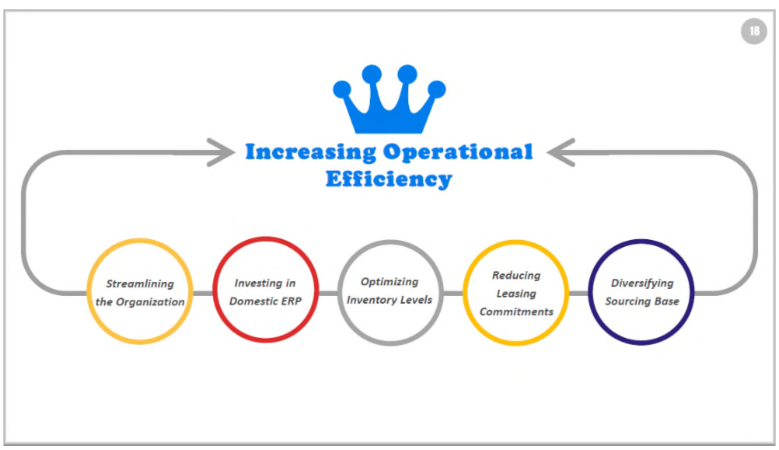
152. Further, starting in June 2022, COO Sansone was regularly present at the Buckeye warehouse to address problems and discuss the distribution backlog with Tarnosky, walking the DC floor and speaking to warehouse associates regarding their activities. Sansone spent at least one to two weeks per month from June to August 2022 at the DC. Even a casual observer at Buckeye could tell that the DC was over capacity and not able to operate with even close to the necessary productivity: "missing" inventory was stacked across wide swathes of the warehouse floor, pallets of incomplete orders were stored while they awaited additional product to be unloaded, and hundreds of trailers and shipping containers were parked in the lot waiting to be unloaded. Undoubtedly, Sansone reported back to Perlmutter, and most likely to Fall Jung, what he was seeing. Perlmutter himself visited the Buckeye DC on at least one occasion during 3Q22.

153. Finally, Defendants admitted that the ERP implementation, inventory management and the consolidated DC were cornerstones of their operations:

(a) A May 2022 investor relations presentation highlighted: "Investing in Domestic ERP," "Optimizing Inventory Levels," and "Reducing Lease Commitments" as three of the five elements of Funko's plan to increase operational efficiency.



(b) At the Company's September 13, 2022 investor day, Fall Jung stated that "improved operating margin," as a result of the DC and ERP would allow the Company to meet its touted adjusted EBITDA margin goal of 20% by 2026: "And improved operating margin. So

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with our new DC, we feel we can improve our overall operating cost and leverage by streamlining our logistics . . . and our ERP will be instrumental";

(c) Perlmutter made clear at the September 13, 2022 investor day that the ERP would be critical to developing the Company's growing direct-to-consumer e-Commerce business: "So what we've talked about as far as our current investments are somewhat locked into the ERPs. The ***ERP is step #1***. And then the e-commerce platform is #2"; and

(d) On November 3, 2022, Perlmutter referred to the DC and ERP system as "critical to service our near-term demand as well as support our long-term growth objectives."

B. Analysts and Investors Frequently Asked Questions About, and Defendants Frequently Evinced Personal Knowledge by Commenting on, Funko's Infrastructure Project Costs and Inventory Management

154. Throughout the Class Period, Perlmutter and Fall Jung were asked specific, direct questions by Wall Street analysts about the Company's inventory management as well as the levels and timing of costs related to the DC and ERP infrastructure projects, and they held themselves out as knowledgeable about these topics. For example:

(a) On March 3, 2022, an analyst asked: "You gave 80 basis points of pressure from – it seems like more of a transitory DC and ERP implementation and transition. Any context on when that 80 basis points is concentrated? Is it first half, second half? Anything we should be mindful of?" Fall Jung answered: "Yes. ***Yes, first half, for sure***. [W]e will probably launch in the beginning early the Q3 [sic] for the ERP, but the distribution center move will happen in the first half."

(b) On May 5, 2022, an analyst asked, Fall Jung "on your remarks around the onetime project spend for ERP and DC (inaudible) can you just help us think through the total amount that you anticipate spending? And then anything more by cadence by quarter would be really helpful." Fall Jung replied:

> So yes, we reported out that was about 80 basis points on the year, ***all of which will happen in the first half of the year***. It's about 2 points of pressure just in Q2 on adjusted EBITDA. So we're launching – or we did launch the new DC in April, and the ERP is set to come out at the end of the quarter.

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The analyst followed-up: "So anything trickling into the back half? Or should we assume that it's pretty much done after Q2?" Fall Jung stated: "It's really the pressures [sic] all in the first half of the year, specifically Q2."

(c) On August 4, 2022, an analyst asked Fall Jung: "Just to give you a chance to talk a little bit more about where the inventory resides, how much of it is related to the DC relocation? How much might be in transit? If you could just dimensionalize inventory for us, that would be appreciated." Fall Jung stated:

> Yes, inventory, so what we actually ended up, as you know, in Q4, had a lot of delays that rolled into Q1 just due to the congestion within the supply chain. And you're seeing a little bit of that in Q2 as well. Although as we're now looking into the back half of the year, we feel the inventory is in a really good healthy position, and we're poised to deliver on our back half results. It was really about just managing through the congestion that we saw so far. Knowing that, we're seeing those transit times come down and delivery dates to be more on time than they had earlier in the year So there is a large portion of the in-transit, but we're working to get that into the DC and get that out to our customers.

(d) During the same August 4, 2022 call, another analyst asked: "And also on the cost side, you've talked about pushing out this ERP initiative into 2023. Does that mean there's going to be less associated SG&A costs associated with that in 2022?" Fall Jung replied:

> No, and that's actually a great question. There'll be puts and takes about 2022. We will still continue to work on these initiatives throughout the year. So the run rate will continue. But there's other offsetting factors to that. So we don't see it as a major headwind in 2022 so far, but we feel good we made the right decision for the business to not have business interruption as we go into the holiday season."

(e) On November 3, 2022, an analyst asked: "And are you – do you think you're going to have to take any actions on any of your owned inventory – and how does that change how you're thinking about – or does it change how you're thinking about growing the top line double digit?" Fall Jung answered:

> As we think about our inventory, yes, it is up year-over-year. Remember, last year was a pretty tight inventory environment because we were dealing with the supply chain challenges. So there is a little bit of nuance in the number underneath the covers. That being said, we are constantly looking at the quality of our inventory,

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> and we think it generally is very healthy right now. And in the event where we have seen a pullback a little bit in Q4, we have been making the right edits to our inventory, whether it be cutting receipts or pushing receipts out to make sure that we are managing this and managing it down towards the end of the year.

(f) On November 3, 2022, Perlmutter was asked: "And then when do you expect the ERP software system to be rolled out? And should this – if it's in the middle of next year or should this pressure – should you get this pressure back in the second half of next year?" Perlmutter stated:

> On the SG&A and the additional costs with the growth and the infrastructure that we're having to invest in to support the growth. We would expect that to be middle of next year. We are pushing hard to get that ERP up and running, which also, by the way, brings the software to optimize our warehouse which – we built a warehouse to run on WMS. And because of the ERP delay, that's pushing back at WMS. So we've obviously found a lot of manual work around especially to get the record 37% product out last quarter where they continue to do so until we get this up and running, which is, like I said, middle of next year is what we're looking at.

C. Defendants' History of and Receipt of Warnings Concerning Similar Misconduct Support a Strong Inference of Scienter

155. Defendants Perlmutter and Fall Jung were senior executives at Funko (President and CFO, respectively) when, in 2019, the Company accumulated more than ten to twelve million obsolete units of product in its Washington warehouses that interfered with the Company's ability to unload new product from shipping containers. Ultimately, the Company had to write down $16.8 million in inventory, and the share price dropped 40% on the announcement. Simply put, Defendants knew that managing dead inventory was an important element of Funko's operations, that investors considered the information material, and that the failure to do so could have significant financial consequences. More, they knew that failing to disclose the accumulation of dead inventory while warning that they ***could*** have to hold inventory for long periods of time may violate the federal securities laws, as the Hon. Virginia A. Phillips of the Central District of California permitted §10(b) claims against them to proceed based on a substantively identical risk

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warning as is pled in ¶¶114, 123, 128 and 143, here.[8] Defendants settled the case for $7 million dollars following Judge Phillips' ruling. That Defendants were involved in securities fraud litigation regarding some of the very same conduct as alleged above within ***six months*** of the start of the Class Period further supports a strong inference of scienter.

D. The Removal of Fall Jung and Perlmutter from the C-Suite Supports a Strong Inference of Scienter

156. That Fall Jung was fired and Perlmutter demoted back to a sales role further supports an inference that they had direct knowledge of the true facts concealed regarding Funko's foundering operations and snowballing costs during the Class Period. Funko and once-again CEO Brian Mariotti both made clear that the abrupt changes in management were directly related to the events alleged herein.

157. For example, on December 8, 2022, D.A. Davidson reported on a conversation it had with Mariotti following the December 5, 2022 announcement regarding the management shuffle. D.A. Davidson reported:

> We have heard some investors question why former CEO Andrew Perlmutter was not fired; in Mariotti's view, Perlmutter is a world-class business builder and salesperson, but when the new COO comes on board, he will step aside from a broader operational role and focus on the areas best matching his skill-set.

It also reported learning that:

> After the firing of the executive in charge of global operations, the head of IT (a longtime employee of the company) has stepped in to bring in outside firms to assess the situation regarding ERP implementation; the feedback is positive in that a lot of valuable work has been done, but the scope of the work was way too large (*i.e.*, FNKO was putting in a Mercedes whereas a Honda with leather seats would have been more appropriate) – completion of ERP implementation is expected in summer 2023, and FNKO is also receiving a lot of analysis of how to get product out of the Arizona distribution center.

[8] *Ferreira v. Funko*, 2021 WL 8820650, at *15, *20-*22 (C.D. Cal. Oct. 22, 2021).

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158. More, on the first earnings call following Fall Jung's firing and Perlmutter's demotion (March 1, 2023), Mariotti made a point of commenting that Funko's operations had "disrupted our financial and operating performance to an unacceptable degree" and that "[o]ur Board and our management team are deeply focused on execution. . . . To begin, we have strengthened our leadership team."

VII. LOSS CAUSATION/ECONOMIC LOSS

159. At all times during the Class Period, the market for Funko Class A common stock was open, well-developed, and efficient. Throughout the Class Period, Funko Class A common stock traded at artificially inflated prices as a direct result of Defendants' scheme and materially false and misleading statements and omissions of material fact, which were widely disseminated to the securities market, investment analysts, and the investing public. Plaintiffs and other Class members purchased or otherwise acquired Funko Class A common stock relying upon the integrity of the market price of Funko Class A common stock and market information relating to Funko, and have been damaged thereby.

160. When the relevant truth and its impact on Funko's financial results and prospects entered the market through a series of partial disclosures, the price of Funko Class A stock significantly dropped, as the artificial inflation came out of the stock price over time. As a result of their purchases of Funko Class A stock during the Class Period, Plaintiffs and other Class members suffered economic loss, *i.e.*, damages, under the federal securities laws.

161. The corrective impact of each partial disclosure during the Class Period, however, was tempered by Defendants' misleading statements and omissions that continued to conceal the true nature and impact of Defendants' fraud. Each partial disclosure did not on its own fully remove the inflation from Funko's stock price because it only partially revealed the nature and extent of the fallout from Defendants' previously concealed misconduct. Defendants' ongoing misrepresentations and omissions maintained the price of Funko Class A common stock at

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artificially inflated levels, inducing Class members to continue purchasing artificially inflated shares in Funko even after Defendants' partial disclosures.

162. The disclosures that corrected the market price of Funko Class A shares are detailed below. These stock price declines were due to firm-specific, fraud-related disclosures and not the result of market, industry, or firm-specific non-fraud factors.

163. On August 4, 2022, Funko issued a release on Form 8-K and its 2Q22 Form 10-Q announcing its financial results for 2Q22. While the Company reported 2Q22 adjusted earnings per diluted share of $0.26, which exceeded analyst consensus of $0.23, and increased its FY22 revenue and EPS guidance, its gross margin had contracted ***640 bps*** to 32.7%, well below the market consensus of 34.5%. It also announced inventories up 170.9% year over year purportedly due to receipt of inventory that had been delayed in transit. Funko also revealed that it had decided to delay the remaining steps of its ERP implementation until 2023. However, on the post-Market close earnings call that day, Fall Jung misleadingly attributed the decision to the Company "not want[ing] to impair the momentum that we have today," and reassured analysts and investors that though inventory was up, it was "high quality and leave[s] us well positioned to meet our consumer demand and support our strong second half growth forecast."

164. As a result of the August 4, 2022 disclosures discussed above, Funko's Class A share price declined by $4.88, or approximately 18%, on unusually high volume – dropping from a closing price of $26.69 on August 4, 2022, to close at $21.81 on August 5, 2022. This decline removed some of the artificial inflation caused by Defendants' material misstatements and omissions, and caused Plaintiffs to suffer losses. Funko's stock price remained inflated, however, because Defendants continued to conceal the true nature and extent of Funko's operational problems and how they would impact Funko's second half of 2022.

165. Analysts were disappointed that Funko's results were not as robust as expected; as Truist put it in its August 5, 2022 report: "All told, FNKO delivered decent but not great 2Q results . . . shares are likely to trade lower on Friday's open given the relatively bullish sentiment into

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print." And while they were surprised by Funko's gross margin and attention to inventory levels sharpened, they accepted Defendants' representations that those were transitory issues (including the onetime warehouse relocation costs) and that the second half of 2022 would see far better figures. For example, J.P. Morgan noted in its August 5, 2022 report that "the company expects its gross margin to improve sequentially throughout the remainder of the year as it begins to lap the freight cost increases while spot rates also continue to moderate," and that "the company noted its higher inventory balance is driven primarily by transit delays and believes its owned inventories are in a healthy position." In arguing that Funko's prior margin guidance was still realistic, Jefferies emphasized that "FNKO relocated its largest DC from higher-cost Washington to lower-cost Arizona in Q2 and bore 200bps of duplicative costs. . . . Inventory levels reflect in-transit costs, higher shipping rates, and elevated DC costs, which will moderate and overall levels are expected to align with sales growth exiting Q4."

166. On November 3, 2022, Funko issued a release on Form 8-K[9] and its Form 10-Q for 3Q22 announcing unexpectedly poor 3Q22 financial results. While 3Q22 net sales increased to $366 million, 3Q22 adjusted earnings per diluted share of $0.28 was far below analyst expectations of $0.52, adjusted EBITDA fell 11% to $35.7 million (consensus expectations had been $49 million), and SG&A expense in 3Q22 was $97.9 million (26.8% of net sales), an increase of 63.5% year over year and significantly higher than both analyst expectations ***and*** 18% higher than the Company's 2Q22 spending on SG&A (the quarter Fall Jung had promised the SG&A "pressure" would be concentrated). According to the release, SG&A expenses "were higher than expected due to increased infrastructure investment to accommodate recent rapid growth and provide capacity for sustained future growth." The Company's net income decreased nearly 40% compared to 3Q21, while its net income margin contracted 390 bps to 3.0% and its adjusted

[9] This was soon superseded by a release on Form 8-K/A the same day, which decreased the guidance for full year adjusted net income by $8 million and decreased the expected adjusted earnings per diluted share by $0.15.

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EBITDA decreased 11.2%. Inventory at the end of 3Q22 was $265.8 million, up nearly $32 million over the prior quarter and 88.7% over the prior year.

167. The Company also reduced its 2022 financial guidance, indicating in its November 3, 2022 Form 8-K/A that adjusted earnings per diluted share was expected to be only $0.70-$0.80, rather than the previously guided $1.88-$1.99, and expected adjusted EBITDA margin would only be in the "high single digits," not the previously guided 14.6%.

168. The Company's Form 10-Q also disclosed for the first time that the Company had material weaknesses in its internal control over financial reporting stemming from ineffectively designed and implemented user access controls and segregation of duties controls within information technology systems utilized by the Company in its financial reporting – a weakness present in the Company's inventory tracking systems at the Buckeye DC.

169. On the Company's November 3, 2022 earnings call held just prior to market close, Perlmutter disclosed that the Company's "upgraded" warehouse, while "opened" in 2Q22, had been operated since then without the warehouse management software it was designed to operate with. Fall Jung further explained that operating the warehouse without the intended software had resulted in higher labor costs and necessitated "additional machinery to support product movement." Fall Jung also revealed that the Company had added third-party logistics warehouses in order to house inventory and that, all together, the additional investments had reduced adjusted EBITDA that quarter by approximately $5 million. She maintained that while "[i]nventory levels remain higher than the prior year . . . our inventory is generally high quality, we will continue to work through our inventory levels and expect to make sequential progress." However, Fall Jung also disclosed that the SG&A "investment impact on our margin profile" was expected to "largely persist until the completion of our software upgrade next year."

170. Following Defendants' disclosures, Funko's Class A stock price plummeted a staggering ***59%*** on exceptionally high volume, closing at $7.92 per share on November 4, 2022, from a previous day close of $19.50. Defendants' disclosures removed a significant portion of the

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artificial inflation caused by their concealment of Funko's operational problems and causing Plaintiffs to suffer losses. Not all inflation was removed, however, because Defendants continued to conceal the full extent of the problems at Funko's warehouses and the true cost of remediating those problems.

171. Like investors, market analysts were floored by the Company's revelations, and it was evident that they didn't believe Funko management was caught off guard by the increased expenses. For example:

- Truist downgraded Funko's shares to Hold from Buy, stating "[w]hile we normally hesitate to make a reactive ratings downgrade on a stock that's indicating down ~30% in after[-]hours trading, ***tonight's commentary/guidance was inexplicable***, to us. . . . Not only do we have little faith in FNKO's current guidance, but swelling inventory levels (+88%YoY) and higher costs . . . will effectively impair any type of visibility well into '23. Further, and perhaps more importantly, we believe a credibility issue will weigh on shares for the foreseeable future."
- On November 4, 2022, D.A. Davidson asserted that "***[i]t feels like we were hit with a bomb***," and "***[w]e think FNKO should have made disclosures at its [September 2022] investor day, and our frustration is high***[.]"
- On November 4, 2022, J.P. Morgan downgraded the stock from Overweight to Neutral, noting that "the EPS cut was contrary to our preview and far worse than bearish expectations," and that "[w]hile the company suggests direct sales are strong and the implied 4Q sales miss represents retail de-stocking, we view this as the glass half full view and highlight the 'unexpected cost pressures' related to its infrastructure challenges as showing a lack of operational visibility, while the expected margin recovery was a key underpinning to our June upgrade."
- On November 4, 2022, Jefferies commented that Funko was suffering from "Self-Inflicted Wounds: Aside from macro, [management] continues to deal with issues related to an ERP integration & warehouse consolidation . . . we agree with the complaints that these [near term] issues are harder to swallow following a very upbeat investor day less than two months ago."
- On November 7, 2022, Bank of America Global Research downgraded Funko stock to Neutral from Buy, and lowered its 2023 EPS expectation from $2.20 to $1.65, "to reflect ongoing SG&A headwinds on operational challenges from the lack of new ERP/Warehouse management software which expect to persist thru 1H23."

172. On March 1, 2023, the Company announced its disastrous 4Q22 financial results. In 4Q22, net income decreased 368% over prior year to ($46.7) million, with a net loss margin of

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(14%). Adjusted EBITDA was $(6.3) million, while Adjusted EBITDA margin was (1.9%). SG&A expenses in 4Q22 were an outstanding ***$139.2 million***, including ***a $32.5 million*** write-down of capitalized costs associated with the Company's decision to abandon its previously disclosed enterprise resource planning system.

173. The FY22 results announced at the same time were lackluster. While net sales were $1.3 billion, net income was ($5.2) million, Adjusted EBITDA was down 35% year-over-year to $97.4 million, net income margin had contracted ***699 bps*** to (0.4%), and Adjusted EBITDA margin decreased ***720 bps*** year-over-year to 7.4%. Adjusted earnings per diluted share was just $0.57 – a far cry from the $0.70-$0.80 guidance provided on November 4, 2022 (with just two months left in the year).

174. 2023 full-year guidance was also disappointing. In its release, the Company announced that it would be focusing on "gross margin opportunities, fulfillment costs, and other SG&A . . ." but that fixing the Company's existing distribution center and inventory problems "will take several quarters in some cases," and as a result, Adjusted EBITDA for the year was only expected to be between $50 and $75 million, rather than the $129 million analysts had anticipated. And, despite prior assurances that the excess inventory in the Company's warehouse was "high quality" and would be sold, the Company disclosed that it intended to take a write down of approximately ***$30 to $36 million*** to eliminate excess inventory in the first half of 2023 in order "to reduce fulfillment costs by managing inventory levels to align with the operating capacity of our distribution center."

175. During the earnings call later that day, Mariotti admitted that to "deliver reliable, profitable growth . . . we will need to reset our operational foundation." Mariotti acknowledged that Funko's excess inventory "volume [was] restricting our distribution center's throughput and incurring incremental container rental charges" and that to "deliver reliable, profitable growth . . . we will need to reset our operational foundation." New CFO and COO Steve Nave acknowledged that "the systems side" "is really the biggest hamstring in our U.S. distribution" and that the

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Company had decided to abandon its years-long ERP implementation and pivot instead to a warehouse management system in order to staunch the Company's bleeding of cash through its distribution center. And tellingly, when an analyst asked Nave: "[N]ow that you've stepped into this role and you had a look under the hood, do you have confidence in Funko's systems and ability to track that inventory?", Nave effectively said ***no***:

> My confidence level, yes, ***we don't have the best systems right now***, which is why we talked about things like an ERP and a warehouse management system. So ***I have confidence that we're going to get to a place*** where our systems infrastructure supports the business the way it needs to.

176. Following these disclosures, artificial inflation introduced by Defendants' concealment of their operational problems through false and misleading statements and omissions left Funko's Class A stock price. From a closing price of $10.70 on March 1, 2023, the stock price fell 7% to close at $9.94 on March 2, 2023. As a result of the artificial inflation leaving Funko's stock, Plaintiffs and other Class members suffered losses.

177. Analyst commentary following the disclosures was focused on Funko's operational issues. For example, Jefferies noted in its March 2, 2023 report that: "As we worried about in our recent downgrade, ***a second shoe did drop*** as the company identified further issues with ERP/inventory. 1Q23 and FY23 guidance came in below consensus . . . ." J.P. Morgan stated in its March 2, 2023 report that,

> [o]verall, it is clear the new management team is acting swiftly to fix the operational issues and restore credibility with investors (with the guidance reset and increased transparency important first steps). ***However, as expected, the operational issues appear more severe than originally expected with the warehouse management system roll out this summer only providing a quick fix and the ERP implementation pushed to 2024***.

(Emphasis in original). Writing on March 23, 2023 following a conversation with Funko management at D.A. Davidson's 6th Annual Consumer Growth Conference, D.A. Davidson stated: "Management is very aware that when 1Q23 is reported, investors will want to hear specific evidence that operations are getting better and not worse."

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VIII. APPLICABILITY OF THE PRESUMPTION OF RELIANCE AND THE FRAUD-ON-THE-MARKET DOCTRINE

178. Plaintiffs will rely, in part, upon the presumption of reliance established by the fraud-on-the-market doctrine in that: (i) Defendants made public misrepresentations or failed to disclose material facts during the Class Period; (ii) the omissions and misrepresentations were material; ((iii) Funko's Class A common stock traded in an efficient market; (iv) the Company's Class A common stock was traded on the Nasdaq and was covered by multiple analysts; and (v) Plaintiffs and members of the Class, purchased, acquired, and/or sold Funko Class A common stock between the time Defendants failed to disclose or misrepresented material facts and the time the true facts were disclosed, without knowledge of the omitted or misrepresented facts.

179. Based on the foregoing, Plaintiffs and the members of the Class are entitled to a presumption of reliance upon the integrity of the market.

180. Plaintiffs and the members of the Class are entitled to the presumption of reliance established by the Supreme Court in *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972), as Defendants omitted material information in their Class Period statements in violation of a duty to disclose such information, as detailed above.

IX. NO SAFE HARBOR

181. The federal statutory "safe harbor" or bespeaks caution doctrine applicable to forward-looking statements under certain circumstances do not apply to any of the false and misleading statements pleaded in this Complaint. Many of the specific statements pleaded here were not identified as "forward-looking statements" when made, but were instead statements of purportedly current facts and conditions at the time the statements were made, including statements about Funko's business operations.

182. To the extent that any of the false and misleading statements alleged herein were forward-looking, those statements were not accompanied by meaningful cautionary language identifying important facts that could cause actual results to differ materially from those in the

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statements. As set forth above in detail, then-existing facts contradicted the statements by the Defendants regarding Funko's infrastructure projects, inventory management, and SG&A spending, among others. Given the then-existing facts contradicting the statements by the Defendants, any generalized risk disclosures made by Funko were not sufficient to insulate the Defendants from liability for their materially false and misleading statements.

183. To the extent that the statutory safe harbor does apply to any forward-looking statements pleaded herein, Defendants are liable for those false forward-looking statements because at the time each of those statements was made, the particular speaker knew that the particular forward-looking statement was false, and the false forward-looking statement was authorized and approved by Funko executives who knew the statement was false when made.

X. CLASS ACTION ALLEGATIONS

184. Plaintiffs bring this action as a class action pursuant to Federal Rule of Civil Procedure 23(a) and (b)(3) on behalf of a Class consisting of all those who purchased Funko Class A common stock during the Class Period, and who were damaged thereby. Excluded from the Class are Defendants, the officers and directors of the Company, the FAH Holders, the TCG Investor Consortium, and members of their immediate families and their legal representatives, heirs, successors, or assigns, and/or any entity in which Defendants have or had a controlling interest.

185. The members of the Class are so numerous that joinder of all members is impracticable. Throughout the Class Period, Funko common stock was actively traded on the Nasdaq, with a public float of more than 25 million shares of Class A common stock as of March 3, 2022. While the exact number of Class members can be determined only by appropriate discovery, Plaintiffs believe that there are likely thousands of Class members that are geographically dispersed, if not more. Record owners and other members of the Class may be identified from records maintained by Funko or its transfer agent and may be notified of the

pendency of this action by mail, using the form of notice similar to that customarily used in securities class actions.

186. Plaintiffs' claims are typical of the claims of the members of the Class, as all members of the Class were similarly affected by Defendants' wrongful conduct in violation of federal law, as alleged herein.

187. Plaintiffs will fairly and adequately protect the interests of the members of the Class and have retained competent counsel with extensive experience in securities class action litigation. Plaintiffs have no material interests antagonistic to or in conflict with those of the Class.

188. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable. Furthermore, as the damages suffered by individual Class members may be relatively small, the expense and burden of individual litigation make it impossible for members of the Class to individually redress the wrongs done to them. There will be no difficulty in the management of this action as a class action.

189. Common questions of law and fact exist as to all members of the Class and predominate over any questions solely affecting individual members of the Class. Among the questions of law and fact common to the Class are:

(a) whether the federal securities laws were violated by Defendants' acts as alleged herein;

(b) whether Defendants' publicly disseminated statements to the investing public during the Class Period omitted and/or misrepresented material facts;

(c) whether Defendants acted knowingly or with severe recklessness in omitting and/or misrepresenting material facts;

(d) whether the price of Funko Class A common stock was artificially inflated during the Class Period due to the material nondisclosures and/or misrepresentations alleged herein; and

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(e) to what extent the members of the Class have sustained damages, and if so, the appropriate measure of damages.

XI. CLAIMS FOR RELIEF

COUNT I

For Violation of §10(b) of the Exchange Act and Rule 10b-5 Against All Defendants

190. Plaintiffs repeat and reallege each and every allegation set forth above as if fully set forth herein.

191. Defendants violated §10(b) of the Exchange Act and Rule 10b-5 by:

(a) employing devices, schemes, and artifices to defraud;

(b) making untrue statements of material fact or omitting to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(c) engaging in acts, practices, and a course of business that operated as a fraud or deceit upon Plaintiffs and other members of the Class in connection with their purchases of Funko common stock.

192. Pursuant to the above wrongful course of conduct, each of the Defendants participated directly or indirectly in: (a) a scheme to defraud; and (b) the preparation and/or issuance of the quarterly and annual reports, SEC filings, releases, and other statements described above, including statements made to securities analysts and the media that were designed to influence the market for Funko common stock. Such reports, filings, releases, and statements were materially false and misleading in that they failed to disclose material adverse information and misrepresented the truth about Funko's operations, finances, and business prospects.

193. By virtue of their positions at Funko, Defendants had actual knowledge of the materially false and misleading statements and material omissions alleged herein and intended thereby to deceive Plaintiffs and the other members of the Class, or, in the alternative, Defendants

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acted with deliberately reckless disregard for the truth in that they failed or refused to ascertain and disclose such facts as would reveal the false and misleading nature of the statements made, although such facts were readily available to Defendants. Said acts and omissions were committed willfully or with reckless disregard for the truth.

194. Information showing that Defendants acted knowingly or with reckless disregard for the truth is peculiarly within Defendants' knowledge and control. As the senior executives and/or directors of Funko, Defendants Perlmutter and Fall Jung had knowledge of the details of Funko's internal affairs.

195. Defendants are directly and indirectly liable for the wrongs complained of herein. Because of their positions of control and authority, Defendants were able to and did, directly or indirectly, control the content of the statements of Funko. As officers and/or directors of a publicly held company, Defendants Perlmutter and Fall Jung had a duty to disseminate timely, accurate, and truthful information with respect to Funko's business, operations, future financial condition, and future prospects. As a result of Defendants' misconduct, the market price of Funko stock was artificially inflated throughout the Class Period. In ignorance of the adverse facts concerning Funko's true business and financial condition, which Defendants concealed, Plaintiffs and other members of the Class purchased or otherwise acquired Funko common stock at artificially inflated prices and in doing so relied upon the price of the securities, the integrity of the market for the securities, and/or upon statements disseminated by Perlmutter and Fall Jung, and were damaged thereby.

196. During the Class Period, Funko Class A common stock was traded on an active and efficient market. Plaintiffs and the other members of the Class, relying on the materially false and misleading statements described herein, which Defendants made, issued, or caused to be disseminated, or relying upon the integrity of the market, purchased or otherwise acquired Funko common stock at prices artificially inflated by Defendants' wrongful conduct. Had Plaintiffs and the other members of the Class known the truth, they would not have purchased or otherwise

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acquired said common stock, or would not have purchased or otherwise acquired it at the inflated prices paid. At the time of the purchases and/or acquisitions by Plaintiffs and the Class, the true value of Funko Class A common stock was substantially lower than the prices paid by members of the Class. The market price of Funko Class A common stock declined upon public disclosure of the facts alleged herein to the injury of Plaintiffs and Class members.

197. By reason of the conduct alleged herein, Defendants have knowingly or recklessly, directly or indirectly, violated §10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.

COUNT II

For Violation of §20(a) of the Exchange Act
Against All Defendants

198. Plaintiffs repeat and reallege each and every allegation set forth above as if fully set forth herein.

199. During the Class Period, Defendants Perlmutter and Fall Jung participated in and oversaw the operation and management of Funko, and conducted and participated, directly and indirectly, in the conduct of Funko's business affairs. Perlmutter and Fall Jung exercised control over Funko's operations and possessed the power to control, and did control, the specific activities which comprise the primary violations about which Plaintiffs and the other members of the Class complain.

200. Perlmutter and Fall Jung acted as controlling persons of Funko within the meaning of §20(a) of the Exchange Act. By virtue of their senior management positions as officers and/or directors of Funko, their participation in and awareness of the Company's operations, and their personal knowledge of the statements filed by the Company with the SEC and/or disseminated to the investing public, these defendants had the power to influence and control and did influence and control, directly or indirectly, Funko's decision-making, including the content and dissemination of the allegedly false and misleading statements and other acts in furtherance of a fraudulent scheme.

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201. In particular, as the CEO (Perlmutter) and CFO (Fall Jung), each of these defendants had direct or supervisory responsibility over the day-to-day operations of the Company and, therefore, is presumed to have had the power to control or influence the particular business and/or operating practices and expenditures and deficient control environment giving rise to the securities violations alleged in Count I, and exercised that power.

202. Funko had the power to control and influence Perlmutter, Fall Jung and other Company executives through its power to hire, fire, supervise, and otherwise control the actions of its employees and their salaries, bonuses, incentive compensation, and other employment considerations. By virtue of the foregoing, Funko had the power to influence and control, and did influence and control, directly or indirectly, the decision-making of Perlmutter and Fall Jung, including the content of their public statements.

203. As a direct and proximate result of the Defendants' wrongful conduct, Plaintiffs and other members of the Class suffered damages in connection with their purchases and/or acquisitions of Funko's common stock during the Class Period when the relevant truth was revealed.

204. By reason of the foregoing, the defendants named in this count violated §20(a) of the Exchange Act.

XII. PRAYER FOR RELIEF

WHEREFORE, Plaintiffs pray for relief and judgment, as follows:

A. Determining that this action is a proper class action, certifying Plaintiffs as Class representatives under Federal Rule of Civil Procedure 23 and designating Lead Counsel as Class Counsel;

B. Awarding Plaintiffs and other members of the Class damages together with interest thereon;

C. Awarding Plaintiffs and other members of the Class their costs and expenses of this litigation, including reasonable attorneys' fees, expert fees, and other costs and disbursements; and

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D. Awarding Plaintiffs and other members of the Class such other and further relief as the Court deems just and proper under the circumstances.

XIII. JURY DEMAND

Plaintiffs hereby demand a trial by jury.

DATED: October 19, 2023

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